2025 Income Tax Credit Review

Joint Legislative Income Tax Credit Review Committee

December 2, 2025

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2025 Credit Reviews

- Annually reviews credits as determined in statute
- This year's review includes:
    1) Credit for Employing National Guard Members
    2) Credit for Employment of TANF Recipients
    3) Credit for Contributions to Qualifying Charitable Organizations
    4) Credit for Contributions to Qualifying Foster Care Charitable Organizations
    5) Credit for Contributions by S Corporations to School Tuition Organizations for Low-Income and Displaced/Disabled Students
- All credits listed above were included on the 2020 review schedule

Role of the Committee

- Determine original purpose of credit
- Establish standards for evaluating and measuring success or failure of credit
- After review process, recommend whether credit should be amended, repealed or retained

Standards for Evaluating Credit

- History, rationale and revenue impact of credit
- Benefits of credit in terms of measurable economic development, investments and jobs
- Complexity of credit in terms of application, administration and approval process

Confidential Taxpayer Information

- Statute authorizes DOR to disclose confidential "statistical information" to the Committee, JLBC Staff and Legislative Staff

- DOR considers credit information confidential if:
    - credits were claimed by 3 or fewer taxpayers, or
    - a single taxpayer used more than 90% of total credits

- Tax credits for Contributions to Charitable Organizations and Foster Care Charitable Organizations are the only credits on the 2025 review schedule that do not include confidential information

Issues Affecting Evaluation

- Lack of performance measures

- Certain costs and benefits can be difficult to quantify

Employment of National Guard Members Credit

December 2, 2025

Employment of National Guard Members Credit
- Summary

- Cost – $0 in FY 2025 for the individual credit, as no claims were filed. Due to confidentiality rules the cost of the corporate credit has not been released.

- Purpose – mitigate costs incurred by employers who employ active duty National Guard members.

- Complexity – simple to use and administer

- Performance Measures – none in statute

Employment of National Guard Members Credit
- Description of the Credit

- The credit provides $1,000 per National Guard member that is deployed on active duty, per year.

- Credit is non-refundable.

- Carry forward is 5 years.

Employment of National Guard Members Credit
- Cost of the Credit

- Cost of the individual credit was $0 in FY 15, $0 in FY 18 through FY 20, and $0 in FY 22 through FY 25.
- In FY 16, FY 17, and FY 21, too few individuals claimed the credit for DOR to release any credit information under its taxpayer confidentiality rules.
- The cost of the corporate credit was $8,000 in FY 16 and $0 in FY 23.
- In FY 17 through FY 22, FY 24 and FY 25, too few corporations claimed the credit for DOR to release any credit information.

Employment of National Guard Members Credit
- Benefits to the Arizona Economy

- Impact to the state's economy is likely negligible due to the limited use of the credit.

- Credit may have a small positive impact on the retention and employment prospects of National Guard members insofar as it encourages employers to hire members.

Employment of National Guard Members Credit
- Potential Performance Measures

- The number of employees claiming the credit and the number of National Guardsmen claimed under this credit can both be determined from available data.

- No additional performance measures are suggested.

- Last reviewed in 2020.
  - In 2015, when the Committee last met, it recommended that the credit be continued.

Employment of Temporary Assistance for Needy Families (TANF) Recipients Credit

December 2, 2025

Employment of TANF Recipients Credit
- Summary

- <u>Cost</u> – The individual income credit was repealed in 2021. Due to confidentiality rules, the cost of the corporate credit from FY 2020 through FY 2025 has not been released.

- <u>Purpose</u> – to encourage employers to hire TANF recipients into permanent jobs and reduce their reliance on public assistance.

- <u>Complexity</u> – simple to use and administer with some reporting and record-keeping requirements.

- <u>Performance Measures</u> – none in statute

Employment of TANF Recipients Credit
- Description of the Credit

- Corporate income tax credit for employing TANF recipients.
- TANF is DES' cash assistance program for low-income households.
- Credit is non-refundable; carry forward is 5 years.
- TANF participation has dropped significantly over the last decade. In part, the decline is due to a reduction in the lifetime limit for receiving benefits to 12 months.
  - Adult participation fell from 13,800 in August 2010 to 1,040 in August 2025.

Employment of TANF Recipients Credit
- Description of the Credit

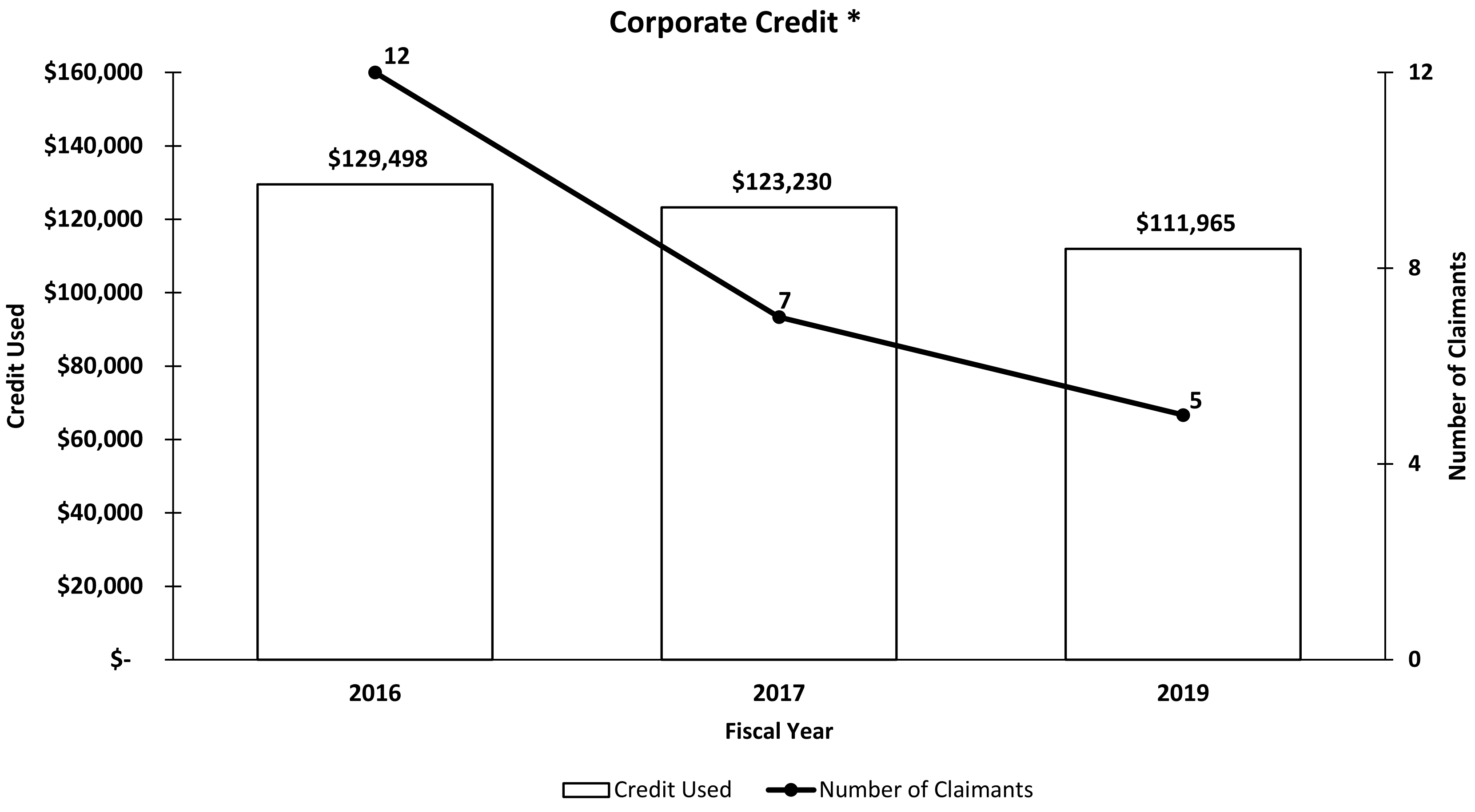
- Credit of up to $500 in the first year of employment, $1,000 in the second year, and $1,500 in the third year.

- Jobs must be full-time and offer wages and benefits comparable to other employees.

- The credit is relatively modest compared to similar federal income tax credits.

Employment of TANF Recipients Credit – No Usage Since FY 19

- Amount of Corporate Credits Taken & Number of Claimants



*DOR did not report number of claimants or amounts of the credit used in FY 2018 or from FY 2020 through FY 2025 due to confidentiality rules.

Employment of TANF Recipients Credit

– Benefits to the Arizona economy

- It is difficult to establish a direct link between the credit and economic development.

- The credit may have a positive impact on the retention and employment prospects of TANF recipients and subsequently reduce reliance on government assistance.

Employment of TANF Recipients Credit
– Potential Performance Measures

- 2- and 3-year retention rates for employees claimed under the credit.

- Last reviewed in 2020. The individual income tax credit was repealed in 2021.
  - In 2015, when the Committee last met, it recommended that both the individual and corporate tax credits be repealed.

Contributions to Qualifying Charitable Organizations (QCO) Credit

December 2, 2025

JLBC

Qualifying Charitable Organizations Credit
- Summary

- Cost – $94.0 million in FY 2025.
  – 190,883 claims

- Purpose – encourage increased cash contributions to charities that help low-income or chronically ill/disabled persons

- Complexity – simple to use and administer

- Performance Measures – none in statute

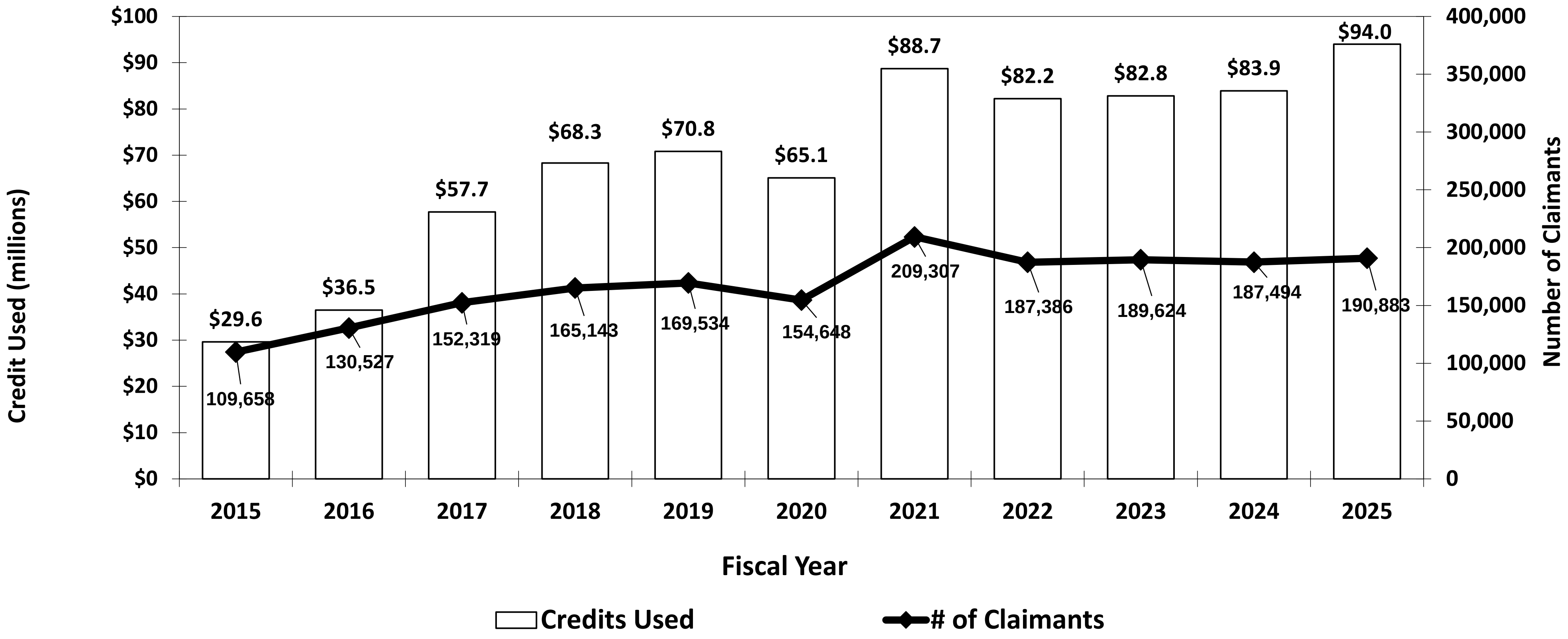
Qualifying Charitable Organizations Credit
- Description of the Credit

- The credit is available to individuals who make cash contributions to qualifying charities.
- Taxpayers do not need to itemize deductions to claim credit.
- For contributions to QCOs, a taxpayer cannot claim both an itemized deduction (or an additional standard deduction) and the QCO credit.
- A QCO is required to:
  - Be a 501(c)(3) or a community action agency
  - Spend ≥ 50% of its budget on services to low-income or chronically ill/disabled
  - Affirm that is does not provide, pay for or provide coverage of abortions

Qualifying Charitable Organizations Credit
- Description of Credit (Continued)

- There are more than 1,000 charitable organizations listed on DOR's website.
- Maximum QCO credit is $495 for singles and heads of household and $987 for married filers. These amounts are adjusted annually for inflation.
- Credit is nonrefundable
- Carry forward is 5 years

Qualifying Charitable Organizations Credit
- Amount of Credits Used & Number of Claimants by Fiscal Year



Qualifying Charitable Organizations Credit
- Benefits to the Arizona Economy

- Available data does not indicate to what extent donations to qualifying charities represent new or additional giving.

- Credit may encourage some donors to reallocate their contributions for tax purposes.

Qualifying Charitable Organizations Credit
- Potential Performance Measures

- Number of Arizona residents benefitting from services provided under QCO credit program.
- Type of services provided, and amounts allocated to such services.
- Last reviewed in 2020.
  - In 2015, when the Committee last met, it recommended that the credit be continued.

Contributions to Qualifying Foster Care Charitable Organizations (QFCO) Credit

December 2, 2025

Foster Care Charitable Organizations Credit
- Summary

- Cost – $31.0 million in FY 2025.
  – 44,474 claims
- Purpose – to encourage cash contributions to 59 foster care organizations.
- Complexity – simple to use and administer.
- Performance Measures – none in statute.

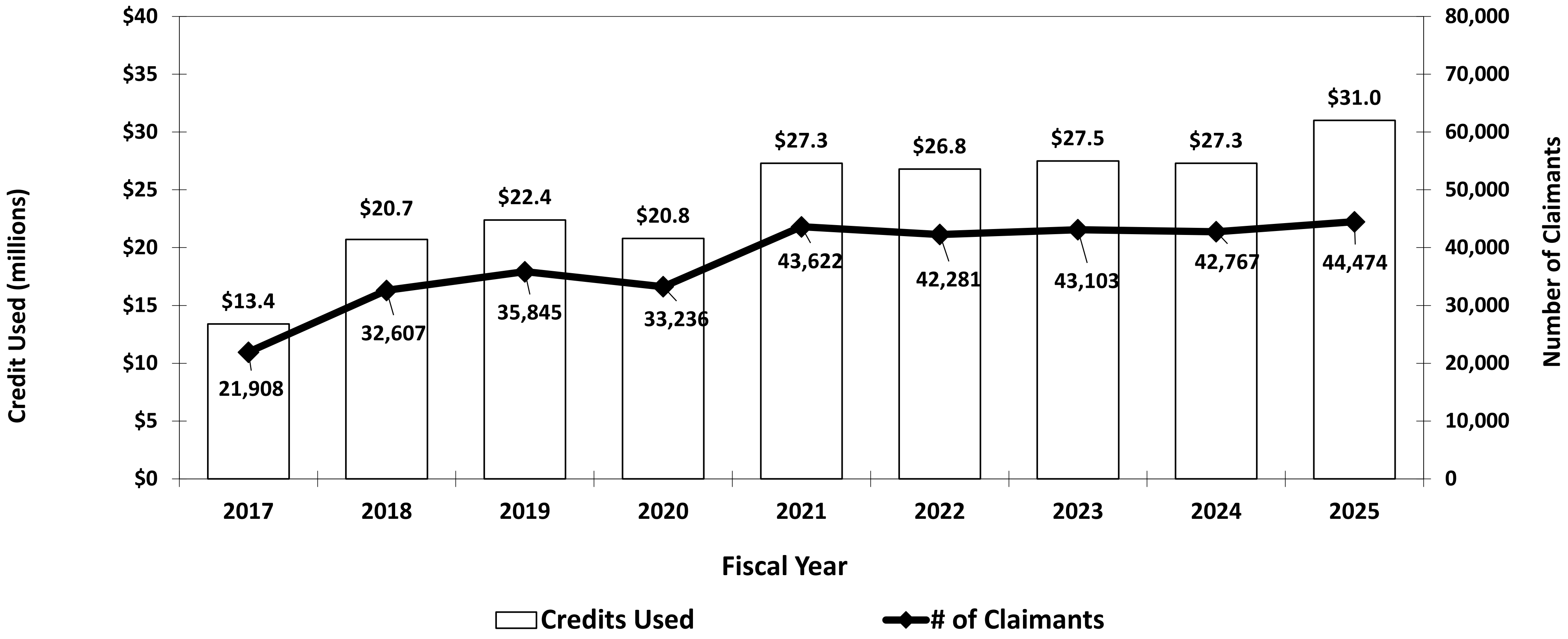
Foster Care Charitable Organizations Credit
- Description of the Credit

- The credit is available to individuals who make cash contributions to qualifying foster care organizations.
- Taxpayers do not need to itemize deductions to claim credit.
- For contributions to QFCOs, a taxpayer cannot claim both an itemized deduction (or an additional standard deduction) and the QFCO credit.
- Maximum QFCO credit is $618 for single filers and heads of household and $1,234 for joint married filers. These amounts are adjusted annually for inflation.
- Credit is nonrefundable with a 5-year carryforward.

Foster Care Charitable Organizations Credit
- Certification Requirements for QFCO’s

- A QFCO must be a Qualified Charitable Organization that provides services to at least 200 children in a foster home or child welfare agency.
- QFCO must direct or spend at least 50.0% of its budget on services for low-income, chronically ill, and disabled residents of the state.
- Services are broadly defined in statute.
- Services include legal services, rent, utilities, behavioral health, and workforce development.

Foster Care Charitable Organizations Credit
- Amount of Credits Used & Number of Claimants by Fiscal Year



Foster Care Charitable Organizations Credit
- Benefits to the Arizona Economy

- Available data does not indicate to what extent donations to qualifying foster care charities represent new or additional giving.

- Credit may encourage some donors to reallocate their contributions for tax purposes.

Foster Care Charitable Organizations Credit
- Potential Performance Measures

- Number of Arizona children in foster care benefitting from services provided under QFCO credit program.
- Type of services provided, and amounts allocated to such services.
- Last reviewed in 2020.
  - However, since the Committee did not meet that year, no recommendations were made.

Pro Rata Credit for Contributions by S Corporations to School Tuition Organizations (STO)

December 2, 2025

Corporate STO "Low-Income Scholarship" Credit
- Summary

- Cost – $17 M in FY 2025 from S Corporations.
  - – Compared to $49 M from C Corporations.
  - – Also reduces state's K-12 costs.
- Purpose – fund "low-income scholarships" for pupils attending private schools.
- Complexity – DOR must pre-approve contributions; each STO must report contribution and scholarship data to DOR annually; "low-income" only.
- Performance Measures – none in statute.

Corporate STO Displaced/Disabled Credit
- Summary

- <u>Cost</u> – $379,100 in FY 2025 from S Corporations.
  - – Compared to $5.4 M from C Corporations.
  - – Actual credit usage may vary.
- <u>Purpose</u> – assist parents with the cost of private school tuition for displaced or disabled pupils.
- <u>Complexity</u> – simple to use for donors. Administration, reporting, and oversight are time-consuming for STOs and DOR because of the number of students and STOs and data quality issues.
- <u>Performance Measures</u> – none in statute.

C Corporations vs. S Corporations

- C Corporations pay corporate income taxes directly on their profits.
  - Shareholders then pay individual income taxes on dividends distributed by the C Corporation.
- S Corporations' profits flow untaxed to the owners, who pay individual income taxes on their pro rata share of these profits.
  - Must meet additional requirements, such as having no more than 100 shareholders and being incorporated/operated domestically.

Corporate STO Credit History

- Prior to 2015, only C Corporations could take either of the Corporate STO Credits.
- Laws 2015, Chapter 301 expanded the Corporate STO Credits to include S Corporations.
- The Committee last reviewed the Low-Income Credit in 2021 and the Displaced/Disabled Student Credit in 2024.
- When enacting Laws 2015, Chapter 301, the statute gave the S Corporate Tax Credits their own unique review dates separate from the C Corporate Tax Credits.