Joint Legislative Budget Committee
Staff Memorandum

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DATE: December 2, 2025

TO: Senator J.D. Mesnard, Chairman, Senate Finance Committee
Representative Justin Olson, Chairman, House Ways and Means Committee

FROM: Hans Olofsson, Chief Economist

SUBJECT: 2025 INCOME TAX CREDIT REVIEW

Each year, the JLBC Staff prepares background materials for the Joint Legislative Income Tax Credit Review Committee as prescribed by A.R.S. § 43-221. At this time, a committee meeting has not been scheduled. Given that our background information may still be of interest, we are now transmitting our material (including a PowerPoint slideshow) for the credits on the 2025 review schedule.

A separate memo provides confidential data on these credits where applicable.

Background

Laws 2002, Chapter 238 established the Joint Legislative Income Tax Credit Review Committee and specified a schedule for review of corporate and individual income tax credits. Pursuant to A.R.S. § 43-222, there are 5 credits scheduled for review in 2025, which are listed below.

Credit Page #

The Joint Legislative Income Tax Credit Review Committee is charged with determining the original purpose of each of the existing income tax credits and establishing a standard for evaluating the success or failure of the credit.

Pursuant to A.R.S. § 43-221, the standard for evaluation of the credits may include: (1) the history, rationale, and revenue impact, (2) the benefit to the state in various economic terms, and (3) the complexity in the use and administration of the credit.

Pursuant to A.R.S. § 42-2003(H), the Department of Revenue (DOR) is authorized to disclose statistical information gathered from confidential tax credit information to this Committee, JLBC Staff and legislative staff. DOR considers tax credit information to be confidential if: (1) 3 or fewer taxpayers claimed the credit, or (2) 90% or more of the total credit used to offset tax liability was taken by 1 taxpayer. All the tax credits on the 2025 review list, except for the Credit for Contributions to Qualifying Charitable Organizations and the Credit for Contributions to Qualifying Foster Care Charitable Organizations, include confidential statistical information.

We have provided a separate memo to the Committee that contains the confidential credit data furnished by DOR. According to DOR, each recipient of this confidential information pursuant to A.R.S. § 42-2003(H) is bound by confidentiality laws and therefore is not to release the information to others. Any discussions regarding this memo must be held in Executive Session.

Limitations

There are certain limitations affecting the evaluation of income tax credits. The lack of performance measures for tax credits is one such example. None of the credits reviewed this year has stated performance measures. Laws 2002, Chapter 238, requires any new credit to include a clause that explains the rationale and objective of the credit (A.R.S. § 43-223).

The evaluation of tax credits in terms of their economic benefits to the state is often difficult to conduct since the data required to do so is rarely available.

2025 Review

The following information is provided (where applicable) for each of the credit categories:

Description - The definition of the tax credit, including how the credit is calculated.

Refundable - Whether the credit is refundable or nonrefundable. A nonrefundable credit can never exceed the taxpayer's tax liability. Instead, any amounts not used to offset the taxpayer's liability in a taxable year either can be carried forward to future tax years or must be forfeited in the same tax year. By contrast, a refundable credit is allowed to exceed the taxpayer's tax liability and any excess amounts are refunded to the taxpayer.

Carry Forward - Whether any unused nonrefundable credit may be carried forward into subsequent tax years, and if so, for how many years.

History and Rationale - The year the tax credit was implemented, revisions to the credit since its enactment, and relevant information regarding the intended purpose of the credit.

Revenue Impact - Based on data reported by DOR, information by fiscal year on the number of claims and the amount of credit used. In addition, the review includes similar information by tax year.

Economic Benefits - A summary of information available related to any economic benefits associated with each tax credit, including economic development, new investments, job creation or retention of existing jobs, and any other economic benefits that may be specific to each credit.
Complexity - Information related to the complexity of administration and application of each tax credit, including the perspective of the state agencies administering the credit, as well as the trade associations and representatives of the corporations and/or individuals claiming the credit.

Potential Performance Measures - A listing of potential measures that might be used to evaluate each of the income tax credits.

The reported information was obtained from a variety of sources. The JLBC Staff reviewed the statutes establishing each of the credits, as well as the tax forms and instructions used by businesses and individuals to claim the credits.

The JLBC Staff also reviewed summaries and minutes of committee and subcommittee hearings that were held prior to adoption of the credits. Various agencies were contacted, including the Department of Revenue.

HO:kp
Attachment
xc: Fletcher Montzingo, Deputy Chief of Staff, Senate
Sean Laux, Senior Policy Advisor, Senate
Molly Graver, Research Staff Deputy Director, Senate Finance Committee
Sean McCarthy, Director of Fiscal Policy, House
Nicole Lovato, Policy Advisor, House
Vince Perez, Senior Research Analyst, House Ways and Means Committee

Credit for Employing National Guard Members

Employment of National Guard Members Credit

Summary

- The credit has been available since January 1, 2006.
- The credit is equal to $1,000 per tax year (TY) for each employee who is placed on active duty by the Arizona National Guard.
- The cost of the individual income credit was $0 in FY 2025.
- The cost and number of corporate credit claims for FY 2025 have not been released by the Department of Revenue (DOR) due to confidentiality rules.
- Very few corporate and individual taxpayers use the credit. The total number of credit claims has gradually decreased from a high of 10 in TY 2010 to a low of 2 in TY 2023.

Statutes

A.R.S. § 43-1167.01 (Corporate) and A.R.S. § 43-1079.01 (Individual)

Description

This credit was last reviewed in 2020. The description of the credit as well as other sections of the credit review have been updated from our 2020 report when relevant.

The statutes provide an income tax credit for corporations and individuals that employ Arizona National Guard members who are placed on active duty. The credit is equal to $1,000 per taxable year, per applicable employee. To qualify for the credit, several more conditions must be met:

- The employees claimed under the credit must be full-time.
- The employee must have served during the taxable year on active duty for training that exceeds the required annual training period, including any activation for federal or state emergencies.

Refundable

The credit is not refundable.

Carry Forward

The unused portion of the credit may be carried forward for a maximum of 5 consecutive years.

History and Rationale

This credit was created by Laws 2005, Chapter 264 and became effective January 1, 2006. According to a purpose statement included in the legislation, the credit was enacted to provide employers with some financial incentive to employ members of the National Guard. Arizona does not offer any other tax incentives for employers of National Guard members.

In the 2005 Legislative Session, Laws 2005, Chapter 115 created the National Guard Relief Fund consisting of donations from private citizens through their state individual income tax return. The monies are used to provide financial assistance to families of National Guard members when they are placed on active duty and are serving in a combat zone. Laws 2015, Chapter 208, however, repealed the National Guard Relief Fund and transferred the remaining balance to the Arizona Department of Veterans' Services for grants to nonprofit organizations that provide financial assistance to Arizona National Guard members and their families.

Revenue Impact

The Department of Revenue (DOR) began reporting individual and corporate income tax credits on a fiscal year basis in FY 2015 and FY 2016, respectively. As reported by DOR, the cost of the individual credit was $0 in FY 2015, FY 2018, FY 2019, FY 2020, and in each year from FY 2022 through FY 2025. In FY 2016, FY 2017, and FY 2021, 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 2016 and $0 in FY 2023. Corporate credit use from FY 2017 through FY 2022, as well as in FY 2024 and FY 2025 has not been reported by DOR as too few corporations claimed the credit in those years.

DOR also reports credit use on a tax year basis. This data is available from 2006, when the credit was first established. It should be noted that this data differs from credit use by fiscal year for several reasons, including filing extensions, amended returns and varied corporate tax years. *Table 1* shows the cost of the corporate tax credit by tax year since the credit's inception in 2006. *Table 2* displays the same information for the individual tax credit.

Table 1

National Guard Members Credit - Corporate Credit Claims by Tax Year

Tax Year	# of Claimants	# of Employees Claimed	Total Credit Available	Credit Used	Carry Forward
2006	3	5	$5,000	$5,000	$0
2007	2	x	x	x	x
2008	5	9	$9,000	$3,100	$5,900
2009	6	9	$14,900	$7,000	$7,900
2010	8	10	$17,900	$17,900	$0
2011	6	8	$8,000	$7,000	$1,000
2012	6	7	$8,000	$6,000	$2,000
2013	5	11	$13,000	$10,050	$2,950
2014	5	4	$6,950	$6,000	$950
2015	3	x	x	x	x
2016	2	x	x	x	x
2017	1	x	x	x	x
2018	1	x	x	x	x
2019	2	x	x	x	x
2020	1	x	x	x	x
2021	1	x	x	x	x
2022	2	x	x	x	x
2023	2	x	x	x	x

# of Claimants – The number of taxpayers who claimed the credit in each year.
Total Credit Available – The total tax credits identified in each tax year, including any new credits and any credits carried over from a previous year and identified in that year.
Credit Used – The total value of credits claimed in each year.
Carry Forward – The total credit identified but not used in each year. The full carry forward may not be reflected in the following year's estimate. For example, a taxpayer could have $400 in a particular credit identified in tax year 2010, use $300 of this amount in 2010 and leave $100 as a carry forward. If this taxpayer did not identify or claim the credit in 2011 the $100 carry forward would not be included in the credit carry forward total for 2011.
x – No data publicly released by the Department of Revenue.

The most recent public data reported by DOR shows an aggregate cost to the state of $6,000 in 2014. The Arizona Department of Emergency and Military Affairs 2024 Annual Report states that 7,466 soldiers and airmen were authorized with the Arizona Army National Guard and Arizona Air National Guard, of which 1,386 are on active duty. If the credit were allowed to be claimed by all National Guard members, including those that are not on active duty, the maximum cost of the credit program would be approximately $7.5 million annually.

Table 2

National Guard Members Credit - Individual Credit Claims by Tax Year

Tax Year	# of Claimants	# of Employees Claimed	Total Credit Available	Credit Used	Carry Forward
2006	1	x	x	x	x
2007	1	x	x	x	x
2008	1	x	x	x	x
2009	2	x	x	x	x
2010	2	x	x	x	x
2011	2	x	x	x	x
2012	3	x	x	x	x
2013	0	x	$0	$0	$0
2014	2	x	x	x	x
2015	2	x	x	x	x
2016	1	x	x	x	x
2017	0	0	$0	$0	$0
2018	0	0	$0	$0	$0
2019	0	0	$0	$0	$0
2020	1	x	x	x	X
2021	0	0	$0	$0	$0
2022	0	0	$0	$0	$0
2023	0	0	$0	$0	$0
2024	0	0	$0	$0	$0

# of Claimants – The number of taxpayers who claimed the credit in each year.
Total Credit Available – The total tax credits identified in each tax year, including any new credits and any credits carried over from a previous year and identified in that year.
Credit Used – The total value of credits claimed in each year.
Carry Forward – The total credit identified but not used in each year. The full carry forward may not be reflected in the following year's estimate. For example, a taxpayer could have $400 in a particular credit identified in tax year 2010, use $300 of this amount in 2010 and leave $100 as a carry forward. If this taxpayer did not identify or claim the credit in 2011 the $100 carry forward would not be included in the credit carry forward total for 2011.
x – No data publicly released by the Department of Revenue.

Economic Benefits

Creation of New Jobs or Retention of Existing Jobs

While this credit may encourage employers to retain existing employees or to take on more employees than they otherwise would have due to the lowered cost of labor, it is unlikely that the credit has had any measurable economic impact to date due to its limited use.

Complexity

The credit does not appear to be unusually complex in its description, calculation or application.

Potential Performance Measures

The number of employers claiming the credit and the number of National Guardsmen claimed under this credit can both be determined from available data. As a result, no additional performance measures are suggested.

Prior Review

The Employment of National Guard Members tax credit was last reviewed by the Joint Legislative Income Tax Credit Review Committee (JLITCRC) in 2020. However, since the JLITCRC did not meet that year, no recommendations were made by the committee. In 2015, when the JLITCRC last reviewed the tax credit in a meeting, the Committee recommended that the credit be continued.

Credit for Employment of TANF Recipients

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

Summary

- The individual income tax credit was repealed in 2021.
- The cost of the corporate credit for FY 2025 has not been released by the Department of Revenue due to confidentiality rules.
- The corporate credit was claimed by a total of 50 taxpayers from Tax Year (TY) 1998 through TY 2023. (Credit information after TY 2023 is not currently available.)
- Between 1998 and 2018, 2,232 positions were claimed under this credit for an average benefit of $1,106 per job. (Information after 2018 is not available.)
- The number of former TANF recipients claimed as new hires decreased significantly – from 408 in TY 2003 to 30 in TY 2017 and 0 in TY 2023. During the same time, the number of TANF recipients has declined significantly.
- The credit supplements similar federal income tax credits. While the state provides up to $500, $1,000, and $1,500 in credits for the first 3 years after hiring a TANF recipient, an employer may also qualify for federal tax credits of up to $4,000 in the first year and $5,000 in the second year.
- It is difficult to determine whether the credit directly results in savings from lower TANF participation. Former TANF recipients may find employment regardless of the income tax credits.

Statutes

A.R.S. § 43-1175 (Corporate)

Description

The credit was last reviewed in 2020. The description of the credit as well as other sections of the credit review have been updated from our 2020 report when relevant.

The statutes provide corporations an income tax credit for employing Arizona residents who are recipients of the low-income TANF assistance program. To qualify for the credit, several more conditions must be met:

- The employees claimed under the credit must be full-time.
- The employer must provide health insurance if coverage is provided to other employees not on TANF.
- The wages must meet or exceed the legal minimum wage and be comparable to wages received by non-TANF employees.
- The TANF employees must be employed for at least 90 days during the first year the credit is claimed.
- Periods for which the employee's wages were subsidized through the Jobs Program as provided by A.R.S. § 46-299 are not allowed to be included as periods of employment. (The Jobs Program is Arizona's mandatory employment and training program for work-eligible individuals in households receiving TANF cash assistance.)
- The TANF employees were not employed by the employer within 12 months before the current hire date.
- The TANF employees were not claimed under any other Arizona employment credit based on wages paid.

The credit is equal to:

- One-fourth of the taxable wages paid to a qualified employee up to a maximum of $500 in the first year of employment.
- One-third of taxable wages up to a maximum of $1,000 in the second year of continuous employment.
- One-half of taxable wages up to a maximum of $1,500 in the third year of continuous employment.

Refundable

The credit is not refundable.

Carry Forward

The unused portion of the credit may be carried forward for a maximum of 5 consecutive years.

History and Rationale

TANF is a federal block grant administered by the Department of Economic Security to provide a variety of assistance to low-income recipients, who are defined by A.R.S. § 46-101 as those who are granted assistance under Section 403 of Title IV of the 1996 Personal Responsibility and Work Opportunity Reconciliation (PRWORA) Act.

The state's TANF employer tax credit was created by Laws 1997, Chapter 300 and became effective January 1, 1998. The statutes creating the tax credits do not include a specific statement of purpose or a rationale. The likely intent was to encourage employers to hire TANF recipients into permanent jobs and reduce their reliance on public assistance.

The state's TANF tax credits were enacted during a time when the federal government was also creating tax incentives to promote the hiring of public assistance recipients. The U.S. Department of Labor, Employment and Training Administration (DOLETA), administers programs related to the Work Opportunity Tax Credit (WOTC), which is authorized by the Small Business Job Protection Act of 1996.

The WOTC is a federal income tax credit that encourages employers to hire 10 targeted groups of job seekers by reducing employers' tax liability by as much as $4,000 per qualified worker in their first year of employment. Two of the targeted groups are Short-Term and Long-Term TANF recipients. Short-Term TANF recipients are those that have received TANF benefits for any 9-month period during the 18-month period ending on the hiring date. Long-Term TANF recipients are individuals that have received TANF benefits for at least 18 consecutive months ending on the hiring date.

The available federal credit is 40% of qualified wages for the first year of employment, up to $4,000 and 50% for the second year, up to $5,000. The WOTC credit, which was extended through the end of 2025, has been continuously renewed since its inception. Notwithstanding the title of the enacting legislation, the WOTC is not restricted to small businesses.

Because the individual credit had gone unused for 3 consecutive years, it was automatically repealed under the Tax Corrections Act of 2021 (Laws 2021, Chapter 196). (Pursuant to A.R.S. § 43-224, if an individual or corporate income tax credit is not claimed by any taxpayer for 3 consecutive years, the credit is automatically repealed.)

Revenue Impact

The Department of Revenue (DOR) began reporting corporate income tax credits on a fiscal year basis in FY 2016. As reported by DOR, the cost of the corporate credit was $129,500 in FY 2016, $123,200 in FY 2017, and $112,000 in FY 2019. The cost of the corporate credit was not reported for FY 2018 and from FY 2020 through FY 2025 due to taxpayer confidentiality rules.

DOR also reports credit use on a tax year basis. This data is available from 1998, when the credit was first established. It should be noted that this data differs from credit use by fiscal year for several reasons, including filing extensions, amended returns, and varied corporate tax years. *Table 1* below shows the cost of the corporate credit by tax year since the credit's inception in 1998. As noted above, the individual credit was repealed in 2021.

As shown in *Table 1*, the number of corporations claiming the credit has gradually decreased over time, from a high of 14 claims in TY 2004 to a low of 0 in TY 2023. The corresponding credit used to offset corporate tax liability decreased from a high of $485,190 in TY 2003 to a low of $0 in TY 2023.

The average caseloads for adult recipients of TANF Cash Benefits have decreased markedly from 120,327 in FY 2003 to 25,878 in FY 2015, and 1,527 in FY 2025. This is due in part to policy changes between FY 2010 and FY 2017 that reduced the lifetime limit for receiving TANF Cash Benefits from 60 months to 12 months.

Table 1, which summarizes the corporate income tax impact of this credit by tax year, was provided by the Arizona Department of Revenue (DOR).

Table 1
Employment of Temporary Assistance for Needy Families (TANF) Recipient Credit - Corporate Credit Claims by Tax Year

Tax Year	# of Claimants	Total Credit Available	Credit Used	Carry Forward
1998	3	$35,325	$35,325	$0
1999	5	$49,653	$47,189	$2,464
2000	6	$41,996	$27,598	$14,398
2001	6	$84,354	$57,851	$26,503
2002	8	$184,997	$173,600	$11,397
2003	9	$472,478	$466,392	$6,086
2004	14	$491,175	$485,190	$3,771
2005	13	$122,183	$99,575	$22,608
2006	11	$51,548	$40,754	$10,794
2007	12	$51,014	$45,014	$6,000
2008	10	$57,956	$28,956	$29,000
2009	12	$129,448	$43,128	$86,320
2010	7	$117,119	$61,239	$56,480
2011	8	$131,480	$64,500	$66,980
2012	9	$161,978	$87,498	$74,480
2013	8	$221,260	$121,998	$90,762
2014	11	$240,649	$131,046	$81,243
2015	6	$155,862	$64,619	$72,173
2016	5	$124,401	$27,100	$86,801
2017	4	$154,988	$88,915	$58,073
2018	4	$109,073	$79,991	$4,350
2019	2	x	x	x
2020	2	x	x	x
2021	1	x	x	x
2022	1	x	x	x
2023	0	$0	$0	$0

# of Claimants – the number of taxpayers who claimed the credit in each year.
Total Credit Available – the total tax credits identified in each tax year, including any new credits and any credits carried over from a previous year and identified in that year.
Credit Used – the total value of credits claimed in each year.
Carry Forward – the total credit identified but not used in each year. The full carry forward may not be reflected in the following year's estimate. For example, a taxpayer could have $1 million in a particular credit identified in tax year 2007, use $400,000 of this amount in 2007 and leave $600,000 as a carry forward. If this taxpayer did not identify or claim the credit in 2008, the $600,000 carry forward would not be included in the credit carry forward total for 2008.
x – No data publicly released by the Department of Revenue.
Italics indicate preliminary numbers.

Economic Benefits

Measurable Economic Development
New Investments
Creation of New Jobs or Retention of Existing Jobs

The economic development or new investment related to this credit cannot be measured with the data available. However, due to the relatively few jobs qualified under this credit program, we believe that the statewide economic impact has been limited. According to DOR, the annual number of employees claimed under the TANF credit has decreased from a high of 408 in 2003 to a low of 0 in 2022.

The state tax credit does not provide a large incentive for prospective employers. However, it may influence a favorable hiring decision on the margin and help to overcome employers' reluctance to provide employment to program participants. By using both the federal WOTC tax credit and the state tax credit, a company could claim up to $4,500 in credit for a new hire in their first year of employment, $6,000 in the second year, and $1,500 in the third year.

To fully assess the net costs and benefits to the state associated with the tax credit, the value of TANF benefits paid to former recipients must be taken into account. In FY 2025, TANF recipients received an average of $120 per month. If an individual were to receive TANF benefits for a full 12 months, the total amount over this period would be slightly less than $1,445.

There would appear to be some savings to the state due to the reduction in TANF expenditures. However, it cannot be determined how many former TANF recipients would have found employment without the existence of the state tax credit. Moreover, as economic conditions change and affect the labor market, some former TANF recipients may return to apply for benefits.

Complexity

The TANF recipient employer credit does not appear to be unusually complex in its description, calculation or application. However, employers are required to keep additional records on qualifying employees and to complete another form to submit with their Arizona tax returns.

Potential Performance Measures

Performance measures could include:

1. 2- and 3-year retention rates for employees claimed under the credit. It appears that DOR has the data needed to make these calculations.

2. The value of wages and benefits paid to TANF recipients that are employed by companies claiming the credit. While the companies would have this information readily available, this measure would require them to compile and report additional data that is not currently required.

3. The growth in compensation for eligible employees that are retained for 2 or more years. This measure also could be obtained from the employers' payroll records but would be an additional reporting burden.

4. The length of unemployment of TANF recipients that are hired by companies claiming the credit. This measure could indicate whether the new hire may or may not have found employment without the benefit of the tax credit.

The statute does not impose any requirements related to these measures.

Prior Review

The credit was last reviewed by the Joint Legislative Income Tax Credit Review Committee in 2020. However, since the Joint Legislative Income Tax Credit Review Committee did not meet that year, no recommendations were made by the Committee. When the credit was reviewed in 2015, the Committee recommended that both the individual and corporate tax credits should be repealed.

Credit for Contributions to Qualifying Charitable Organizations

Contributions to Qualifying Charitable Organizations Tax Credit

Summary

- This credit has been available since January 1, 1998.
- The cost of the credit was $94.0 million in FY 2025.
- The credit was claimed by 190,883 taxpayers in FY 2025.
- Beginning in the 2013 tax year, taxpayers no longer needed to itemize their deduction to claim this credit.
- Since 2016, individuals are allowed separate credits for voluntary cash contributions to Qualified Charitable Organizations and Qualified Foster Charitable Organizations.
- Beginning in 2023, the maximum allowable credit is adjusted annually for inflation. In 2025, the maximum credit is $495 for single filers and heads of households, and $987 for joint married filers.
- There are currently more than 1,000 charitable organizations that qualify for credit eligible donations.

Statute

A.R.S. § 43-1088 (Individual Income Tax)

Description

This credit was last reviewed in 2020. The description of the credit as well as other sections of the credit review have been updated from our 2020 report when relevant.

This credit is provided to taxpayers that make voluntary cash contributions to qualifying charitable organizations (QCO). The credit is available to individuals but not to corporations. Partnerships cannot pass the credit through to their partners, and S corporations cannot pass through the credit to their shareholders. Taxpayers do not need to itemize their deductions to claim this credit. However, an individual <u>cannot</u> claim both a tax credit and an itemized deduction for the amount of contributions made to a QCO. Moreover, an individual <u>cannot</u> claim both a tax credit and the standard deduction increase for charitable contributions to QCO.

To qualify for credit eligible contributions, the charity must be either a tax-exempt 501(c)(3) charitable organization or a designated community action agency that receives community services block grant monies. Additionally, the organization is required to spend at least 50% of its budget on services to Arizona residents who are either: (1) Temporary Assistance for Needy Families (TANF) benefit recipients, (2) low-income persons, or (3) chronically ill or physically disabled (Statute defines "services" as cash assistance, medical care, child care, food, clothing, shelter, job placement, job training, behavioral health, workforce readiness services, workforce development programs, or any other assistance that meets immediate basic needs.) The maximum general QCO tax credit in 2025 is $495 for a single individual or head of household and $987 for a married couple filing a joint return. These amounts are adjusted annually for inflation.

To qualify for credit eligible donations, the charity is required to provide the Department of Revenue (DOR) with a written certification that it meets all the statutory requirements of a QCO. The written certification, which is signed under penalty of perjury, must include a copy of the organization's financial statements showing that 50% of its budget is directed or spent on qualifying recipients and a federal (501)(c)(3) tax-exempt letter (or status as a community action agency receiving block grant monies). The charity must also provide a statement indicating that it does not provide, pay for, or provide coverage of abortions and does not financially support any other entity that provides, pays for or provides coverage of abortions.

In 2013, the QCO credit was expanded to include cash contributions to qualifying foster care charitable organizations (QFCO). A QFCO must meet all the requirements of a general QCO and spend at least 50% of its budget providing services to at least 200 foster children in Arizona. In 2016, a separate credit was created for cash contributions to a QFCO. (The JLBC Staff has prepared a separate review of the QFCO credit.)

Refundable

The credit is not refundable.

Carry Forward

The tax credit may be carried forward for 5 taxable years.

History and Rationale

This credit was created by Laws 1997, Chapter 300 and became effective on January 1, 1998. According to historical records, the credit was added as an amendment in Conference Committee to the omnibus welfare bill (SB 1357) that redesigned Arizona's welfare system to comply with federal welfare reform laws enacted in 1996.

Laws 2005, Chapter 334 increased the maximum credit for married taxpayers filing joint returns from $200 to $400. The maximum credit for single and head of household filers was left unchanged at $200.

Laws 2009, Chapter 80 expanded the credit to include donations to charitable organizations that provide services to chronically ill or disabled children. Additionally, the act restricted the credit to taxpayers itemizing their deductions and eliminated the requirement that a baseline year be established before the credit can be claimed. To qualify for the credit prior to 2009, taxpayers had to itemize their deductions (and specifically include deductions for charitable contributions) on a prior year's state tax return at least once in order to establish a "baseline" year and amount. The credit was calculated based on charitable contributions over and above the baseline amount.

Chapter 80 established a new certification process for QCO as outlined in the *Description* section above. Prior to 2009, charities were not required to submit any supporting documents to DOR, such as financial statements or verification of tax-exempt status. Instead, charities "self-certified" themselves by merely sending a letter to DOR stating that they met all the criteria of a QCO. Beginning in 2018, DOR assigns each QCO a 5- digit identification number that tax filers must list on a form when claiming the tax credit. According to information made available on DOR's website, there are currently more than 1,000 QCOs in the state.

Laws 2009, Chapter 167 provided that individual income taxpayers can authorize their employers to reduce their withholding tax amounts by the amount of the credit claimed. The act became effective in 2010.

Laws 2011, Chapter 55 required a statement that the QCO does not provide, pay for, promote, provide coverage of, or provide referrals for abortions and does not financially support any other entity that provides, pays for, promotes, provides coverage of or provides referrals for abortions.

Laws 2012, Chapter 271 amended Laws 2011, Chapter 55 by removing the requirement that charitable organizations include a statement, which declare that they do not promote or provide referrals for abortion for purposes of the tax credit.

Laws 2013, Chapter 236 removed the requirement that an individual income tax filer itemize deductions in order to claim the tax credit.

Laws 2013, 1st Special Session, Chapter 9 expanded (retroactive to January 1, 2013) the tax credit to include qualifying foster care charitable organizations. A qualifying foster care organization must spend at least 50% of its budget providing services to at least 200 foster children in Arizona.

Laws 2015, Chapter 250 expanded the tax credit to include donations made to QFCOs that provide services to under-21-year-old former foster youth in the Transitional Independent Living program.

Laws 2016, Chapter 109 increased the maximum amount that an individual income taxpayer is allowed to claim for cash contributions to qualifying charitable organizations (QCO) and qualifying foster care charitable organizations (QCFO), beginning in TY 2016. Chapter 109 increased the maximum QCO credit from $400 to $800 for married couples filing joint returns and from $200 to $400 for all other filers. The maximum amount for the QCFO credit was increased from $800 to $1,000 for married couples filing joint returns and from $400 to $500 for all other filers. Additionally, Chapter 109 allows a taxpayer to receive separate credits for cash contributions to a QCO and a QFCO.

Laws 2016, Chapter 309 provides that cash contributions to charitable organizations made on or before April 15th for purposes of claiming the charitable tax credit can be applied to either the current or preceding taxable year.

Laws 2019, Chapter 297 expanded the eligibility criteria for the state charitable tax credit to include organizations that serve both children and adults with chronic illness or disability rather than solely children. Chapter 297 is effective retroactively from January 1, 2019.

Laws 2022, Chapter 385 annually adjusts the maximum allowable credit amounts for inflation, beginning in TY 2023.

Laws 2025, Chapter 257 expands the scope of services an organization can provide and still qualify as a QCO. The definition of a QCO is expanded to include services such as behavioral health, character education programs, workforce development programs, secondary education student retention programs, and housing and financial literacy services. A QCO must submit a written statement to DOR specifying that it will either direct or spend (rather than only spend, as required previously) at least 50% of its budget on services assisting low-income residents. This is a clarifying change that mostly applies to "umbrella organizations" that coordinate and support the work of multiple charities by managing fundraising, providing administrative services, and distributing funds to member charities.

Revenue Impact

The Department of Revenue (DOR) is required to report the use of individual income tax credits on a fiscal year basis. *Table 1* below shows the cost of the credit by fiscal year since DOR began reporting individual income tax credits on a fiscal year basis in FY 2015.

Table 1

Contributions to QCOs Credit by Fiscal Year

Fiscal Year	# of Claims	Credit Used
2015	109,658	$29,553,062
2016	130,527	$36,532,108
2017	152,319	$57,694,127
2018	165,143	$68,262,178
2019	169,534	$70,797,068
2020	154,648	$65,062,141
2021	209,307	$88,659,260
2022	187,386	$82,210,693
2023	189,624	$82,786,435
2024	187,494	$83,912,603
2025	190,883	$94,008,073

# of Claims - the number of taxpayers who claimed the credit each year
Credit Used - the total amount of credits used to reduce tax revenue each fiscal year

DOR also reports credit use on a tax year basis. This data is available from 1998, when the credit was first established. It should be noted that this data differs from credit use by fiscal year for several reasons, including filing extensions, amended returns and varied tax years.

As noted above, this credit is only available to individual income tax filers. The total credit use was $87.2 million in TY 2024, the last year for which data is available. The table below, which was provided by DOR, summarizes the tax revenue impact of the credit by tax year.

Table 2

QCO Credit by Tax Year

Tax Year	# of Claimants	Total Contributions	Total Credit Available	Credit Used	Carry Forward
1998	2,894	$523,501	$481,037	$476,691	$4,346
1999	6,725	$1,237,519	$1,168,515	$1,154,768	$13,747
2000	10,654	$1,897,876	$1,829,205	$1,729,123	$35,581
2001	12,538	$2,332,832	$2,257,673	$2,196,043	$41,852
2002	14,226	N/A	$2,687,900	$2,676,946	Not Available
2003	17,467	N/A	$3,286,100	$3,259,400	Not Available
2004	20,736	N/A	$3,884,600	$3,851,700	Not Available
2005	25,587	N/A	$6,637,500	$6,589,000	Not Available
2006	29,202	N/A	$7,988,039	$7,939,507	Not Available
2007 1/	18,280	N/A	$5,877,831	$5,860,953	Not Available
2008	36,568	N/A	$11,077,991	$11,059,408	Not Available
2009	49,915	$23,095,158	$13,556,228	$12,889,895	$666,333
2010	61,602	$28,502,613	$16,899,920	$16,727,074	Not Available
2011	66,396	$30,720,747	$18,191,993	$18,012,263	Not Available
2012	78,736	$36,430,339	$22,128,648	$21,835,458	Not Available
2013 2/	100,398	$45,025,000	$27,457,025	$24,503,609	Not Available
2014 2/3/	116,225	$55,747,000	$35,790,362	$31,617,855	$4,172,507
2015 2/	130,419	$68,064,000	$41,882,428	$36,796,635	$5,085,793
2016	148,703	$90,087,876	$66,349,084	$58,459,196	$7,594,793
2017	165,525	$104,069,795	$77,783,334	$68,594,148	$8,830,903
2018	164,897	$100,051,921	$80,014,935	$68,644,862	$10,968,030
2019	167,057	$99,977,483	$83,573,904	$70,311,855	$12,707,794
2020	190,526	$104,911,793	$98,374,889	$80,666,670	$17,592,411
2021	189,007	$118,009,936	$101,640,893	$83,496,087	$18,067,880
2022	183,689	$113,677,789	$98,996,844	$79,777,538	$19,143,539
2023	186,050	$120,997,495	$103,685,308	$83,539,590	$20,072,569
2024 4/	176,567	$120,574,521	$106,744,902	$87,211,206	$19,465,698

1/ According to DOR, Tax year 2007 data is understated based on limited reporting information available when individual income tax was converted to a new processing program.

2/ The data for tax years 2013 through 2015 includes both Qualifying Charitable Organization and Qualifying Foster Care Charitable Organization information.

3/ According to DOR, based on a sample review of 2014 credit returns, 89% of the total credit was for contributions made to Qualifying Charitable Organization and 11% went to Qualifying Foster Care Charitable Organizations.

4/ Figures are preliminary.

As shown in the table above, the use of the credit has increased significantly over time; from $0.5 million in TY 1998 to $87.2 million in TY 2024, the last year for which credit data by tax year is available. The increase of the maximum credit for married couples from $200 to $300 in TY 2005 and from $300 to $400 in TY 2006 is evident from the close to 100% increase in credit use over the same 2-year period. Similarly, the elimination of the baseline requirement (for purposes of calculating the credit) in TY 2009 appears to have resulted in another large increase in credit usage. The elimination of the itemization requirement beginning in TY 2013 appears to have resulted in additional credit growth. The $22 million increase in credit use from TY 2015 to TY 2016 is likely the result of the increase of the maximum credit from $200 to $400 for individuals and from $400 to $800 for married couples.

Economic Benefits

New Investments
Creation of New Jobs or Retention of Existing Jobs
Commercial Infrastructure Development

This credit is not directly designed to promote economic development or spur new investments that would result in new jobs. Instead, according to DOR's August 2010 report "Income Tax Credits in Arizona," this credit is one of several tax credits in statute primarily intended to encourage cash contributions to certain target groups in society, such as the working poor or students in private or public schools.

Although this credit was not directly intended to promote economic growth, it may still provide some economic benefits to society insofar as it generates funding to help move individuals from underemployment to economic self-sufficiency. There is no data currently available, however, to quantify such benefits.

Complexity

The credit does not seem to be unnecessarily complex in terms of its application, administration, and approval process. The elimination of the baseline year requirement in 2009 and the removal of the itemization requirement in 2013 appear to have simplified the use of the credit considerably.

Potential Performance Measures

Performance measures could include:

1. A requirement to report on the number of Arizona residents (TANF recipients, low-income persons, chronically ill or physically disabled individuals) that benefit from the services provided as a result of the credit donations.
2. A requirement to report on the specific type of services provided (e.g., cash assistance as opposed to job training) and the amounts allocated to such services from the credit donations.

Prior Review

The Contributions to Qualifying Charitable Organizations tax credit was last reviewed by the Joint Legislative Income Tax Credit Review Committee (JLITCRC) in 2020. However, since the JLITCRC did not meet that year, no recommendations were made by the committee. In 2015, when the JLITCRC last reviewed the QCO credit in a meeting, the Committee recommended that the credit be continued.

Credit for Contributions to Qualifying Foster Care Charitable Organizations

Contributions to Qualifying Foster Care Charitable Organizations Tax Credit

Summary

- The cost of the credit was $31.0 million in FY 2025.
- There were 44,474 claims for this credit in FY 2025.
- Beginning in 2023, the maximum allowable credit is adjusted annually for inflation. In 2025, the maximum credit is $618 for single filers and heads of households, and $1,234 for joint married filers.
- There are currently 59 qualifying foster care charitable organizations in Arizona.

Statute

A.R.S. § 43-1088 (Individual Income Tax)

Description

This credit was last reviewed in 2020. The description of the credit as well as other sections of the credit review have been updated from our 2020 report when relevant.

This credit is provided to taxpayers that make voluntary cash contributions to qualifying foster care charitable organizations (QFCO). The credit is available to individuals but not to corporations. Partnerships cannot pass the credit through to their partners, and S corporations cannot pass through the credit to their shareholders. Taxpayers do not need to itemize their deductions to claim this credit. However, an individual <u>cannot</u> claim both a tax credit and an itemized deduction for the amount of contributions made to a QFCO. Moreover, an individual <u>cannot</u> claim both a tax credit and the standard deduction increase for charitable contributions to QCO.

A QFCO is a qualifying charitable organization (QCO) that each year provides services to at least 200 children placed in a foster home or child welfare agency or to persons under 21 years of age participating in a transitional independent living program. The QFCO is required to spend or direct at least 50% of its budget on services to such children or youth. Statute defines services as "cash assistance, medical care, childcare, food, clothing, shelter, job placement, job training, behavioral health, workforce readiness services, workforce development programs, or any other assistance that is reasonably necessary to meet immediate basic needs and that is provided and used in this state." Besides these requirements, a QFCO must meet all the same requirements as for a QCO, which are outlined below.

A QFCO must also be a charity that is exempt from federal income taxation under section 501(c)(3) of the Internal Revenue Code or is a designated community action agency that receives Community Services Block Grant program monies. The QFCO must spend at least 50% of its budget on services to Arizona residents who receive temporary assistance for needy families (TANF) benefits, to low-income residents of this state and their households, or to individuals who have a chronic illness or physical disability and who are residents of this state. Any entity that provides, pays for, or provides coverage of abortions or that financially supports any other entity that provides, pays for, or provides coverage of abortions is not considered a QFCO for purposes of this credit.

To become a QFCO, a charitable organization must complete an application form and submit it along with required documentation to DOR. If an organization meets all the requirements listed above, DOR will certify it as a QFCO. There are currently 59 QFCOs certified by DOR. Since statute does not define what constitutes "immediate basic needs," it is left to DOR's discretion to determine whether the spending on services by the charity meets the 50% threshold required for certification.

In 2025, the maximum credit for cash contributions to QFCO's is $618 for individuals filing as single or head of household and $1,234 for married couples filing jointly. These amounts are adjusted annually for inflation. The QFCO credit is a separate credit from the QCO credit. Therefore, individuals and married couples may choose to claim one or both credits in the same taxable year.

Refundable

The credit is not refundable.

Carry Forward

The tax credit may be carried forward for 5 taxable years.

History and Rationale

The credit was created by Laws 2013, 1st Special Session, Chapter 9 as an expansion to the Contributions to Qualifying Charitable Organizations (QCO) tax credit. Since the credit was still part of the QCO credit, filers could not separately file claims for contributions to QFCO's. The maximum amount for both credits combined was $800 for married couples filing joint returns and $400 for all other filers. This took effect on January 1, 2013.

Laws 2016, Chapter 109 increased the maximum credit to be claimed by an individual to $500 and to $1,000 for married couples. Chapter 109 also fully separated the credit from the Contributions to Qualified Charitable Organizations (QCO) credit so that individuals and married couples can claim a credit for both contributions to QCO's and QFCO's in the same year.

Laws 2016, Chapter 309 provides that individuals who make cash contributions to charitable organizations prior to April 15th for the purposes of claiming the credit can be applied to either the current or previous tax year.

Laws 2022, Chapter 385 annually adjusts the maximum allowable credit amounts for inflation, beginning in TY 2023.

Laws 2025, Chapter 257 expands the scope of services an organization can provide and still qualify as a QFCO. The definition of a QFCO is expanded to include services such as behavioral health, workforce readiness services, and workforce development programs. A QFCO must submit a written statement to DOR specifying that it will either direct or spend (rather than only spend, as required previously) at least 50% of its budget on services assisting low-income residents. This is a clarifying change that mostly applies to "umbrella organizations" that coordinate and support the work of multiple charities by managing fundraising, providing administrative services, and distributing funds to member charities.

Revenue Impact

The Department of Revenue (DOR) is required to report the use of individual income tax credits on a fiscal year basis. *Table 1* below shows the cost of the credit by fiscal year since DOR began reporting individual income tax credits on a fiscal year basis in FY 2015.

Table 1

Contributions to QFCOs Credit by Fiscal Year

Fiscal Year	# of Claims	Credit Used
2017	21,908	$13,415,652
2018	32,607	$20,654,368
2019	35,845	$22,423,333
2020	33,236	$20,815,829
2021	43,622	$27,314,818
2022	42,281	$26,800,272
2023	43,103	$27,511,410
2024	42,767	$27,272,962
2025	44,474	$31,000,974

# of Claims - the number of taxpayers who claimed the credit each year
Credit Used - the total amount of credits used to reduce tax revenue each fiscal year

DOR also reports credit use on a tax year basis. *See Table 2*. This data is available from tax year (TY) 2016. This data differs from credit use by fiscal year for several reasons, including filing extensions, amended returns and varied tax years.

As noted above, this credit is only available to individual income tax filers. The cost of the credit was $20,550,476 in TY 2019, the last year for which data is available. (This figure is still preliminary and thus likely to be revised). The data included in *Table 2* below, which was provided by DOR, summarizes the tax revenue impact of the credit by tax year.

Table 2

QCFO Credit by Tax Year

Tax Year	# of Claimants	Total Contributions	Total Credit	Credit Used	Carry Forward
2016	26,235	$19,876,877	$18,146,367	$16,334,609	$1,811,758
2017	33,839	$25,893,820	$24,012,278	$21,502,241	$2,510,037
2018	36,440	$26,366,332	$25,398,873	$22,864,438	$2,532,732
2019	36,075	$25,896,068	$25,434,460	$22,609,627	$2,824,833
2020	40,953	$29,368,438	$29,162,430	$25,435,628	$3,726,802
2021	43,431	$32,749,544	$33,435,447	$28,208,242	$5,227,205
2022	41,472	$42,059,308	$32,139,758	$26,386,773	$5,752,985
2023	42,156	$44,324,087	$33,544,532	$26,949,008	$6,595,524
2024 1/	42,093	$60,436,994	$36,437,880	$29,722,739	$6,715,141

1/ Figures are preliminary.

# of Claimants – The number of taxpayers who claimed the credit in each year.
Total Credit – The total tax credits identified in each tax year, including any new credits and any credits carried over from a previous year and identified in that year.
Credit Used – The total value of credits claimed in each year.
Carry Forward – The total credit identified but not used in each year. The full carry forward may not be reflected in the following year's estimate. For example, a taxpayer could have $400 in a particular credit identified in tax year 2016, use $300 of this amount in 2016 and leave $100 as a carry forward. If this taxpayer did not identify or claim the credit in 2017, the $100 carry forward would not be included in the credit carry forward total for 2017.

Economic Benefits

The credit is not directly designed to promote economic development or spur new investments that would result in new jobs. It is meant to incentivize the funding of certain target groups in need of financial assistance and allow taxpayers the discretion to choose which organizations to sponsor.

Complexity

The credit is not unduly complex.

Potential Performance Measures

Performance measures could include:

1. A requirement to report on the number of Arizona children in foster care and individuals under 21 transitioning from foster care that benefit from the services provided as a result of the credit donations.
2. A requirement to report on the specific type of services provided and the amounts allocated to such services from the credit donations.

Prior Review

The Contributions to Qualifying Foster Care Organizations tax credit was last reviewed by the Joint Legislative Income Tax Credit Review Committee (JLITCRC) in 2020. However, since the JLITCRC did not meet that year, no recommendations were made by the committee.

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

Credits for Contributions by S Corporations to School Tuition Organizations

Arizona has two different types of Corporate Income Tax (CIT)/Insurance Premium Tax (IPT) Student Tuition Organization (STO) Tax Credits. One is for low-income students. The Joint Legislative Income Tax Credit Review Committee reviewed the Low-Income Credit in 2021 and is scheduled to do so again in 2026.

The second type of CIT/IPT STO Credit is available to displaced/disabled students. Scholarships from this program may be awarded only to students who lived in foster care at any time prior to graduating from high school or obtaining a GED, or who have been identified at any time as having a disability under federal or state law. This credit was reviewed in 2024 and is on the review schedule again in 2029.

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 main difference between C and S Corporations is how they are taxed. C Corporations pay corporate income taxes directly on their profits (net income) while the profits from S Corporations flow untaxed to the owners, who pay individual income taxes on their pro rata share of these profits.

When enacting Laws 2015, Chapter 301, the statute gave both S Corporate STO Tax Credits their own unique review dates separate from the C Corporate STO Credits. Both the S Corporate Low-Income Credit and the Displaced/Disabled Credit were reviewed in 2020 and are on the review schedule again in 2025.

In FY 2025, the total dollar value of donations for the Low-Income STO Credit was $17 million for S Corporations compared to $49 million for C Corporations. Donations for the Displaced/Disabled STO Credit were $379,100 for S Corporations and $5.4 million for C Corporations.

Please see *Attachment A* for the 2021 C Corporate Low-Income STO Credit review and *Attachment B* for the 2024 C Corporate Displaced/Disabled STO Credit review.

Attachment A

Credit for C Corporation Contributions to School Tuition Organizations

Summary

- Current law authorizes tax credits for 4 different types of corporate or insurer contributions to school tuition organizations (STOs). This review specifically addresses C corporation contributions to STOs awarding "low-income scholarships" (A.R.S. § 43-1183).
- C corporations claimed $20.1 million of the STO low-income credit in FY 2021.
- C corporations, S corporations, and insurers claimed a combined $95.9 million in STO low-income credits in FY 2021.
- The credit may impact K-12 Basic State Aid costs if STO scholarship recipients would have otherwise decided to attend a public school in the absence of a scholarship. In that circumstance, there would be foregone General Fund costs of $7,200 per student.
- Overall, taxpayers claimed $215.7 million in the 4 STO tax credits in FY 2021.

Statute

A.R.S. § 43-1183 and A.R.S. § 43-1504

Description

Current law authorizes tax credits for 4 different types of corporate or insurer contributions to school tuition organizations (STOs):

1. Corporate contributions to STOs awarding "low-income scholarships" (A.R.S § 43-1183),
2. Insurer contributions to STOs awarding "low-income scholarships" (A.R.S. § 20-224.06),
3. Corporate contributions to STOs awarding scholarships to "displaced or disabled" pupils (A.R.S § 43-1184), and
4. Insurer contributions to STOs awarding scholarships to "displaced or disabled" pupils (A.R.S § 20-224.07).

This review specifically addresses the **C** Corporation portion of "corporate/low-income" contributions made pursuant to A.R.S § 43-1183, but also indirectly addresses "insurer/low income" contributions made pursuant to A.R.S. § 20-224.06 because the Arizona Department of Revenue (DOR) typically reports combined data for those two programs. The statutory income tax credit review schedule requires review of the **S** Corporation STO low-income credit in a different year. The Insurance Premium tax credits are not subject to the review process.

This C-Corp credit is provided to corporations for voluntary contributions to STOs. A STO is a nonprofit organization that is exempt from federal taxation and that is required to allocate at least 90% of its revenue for educational scholarships or tuition grants to children to attend non-governmental elementary or secondary schools (A.R.S. §43-1502). A STO may use up to 10% of corporate contributions for administration expenses.

Total corporate plus insurer contributions to STOs for "low-income scholarships" are capped at approximately $142.1 million for FY 2023 pursuant to A.R.S. § 43-1183C1. Because of the cap, STO contributions from corporations and insurers must be pre-approved by DOR to be eligible for a tax credit. For FY 2022, the most recent year for which such data is available, DOR has pre-approved halfway through the year $112.0 million in combined corporate and insurer contributions to STOs for "low-income scholarships." Contributions, however, do not always result in the taxpayer using the credit. For example, the taxpayer may lack sufficient liability to take the credit (see *Table 2*).

Contributions from this credit must only be made available for scholarships or tuition grants to students whose family income does not exceed 185% of the income limit required for a student to qualify for reduced-price lunch under the National School Lunch and Nutrition Acts. In FY 2021, the maximum annual income for a family of four for purposes of STO scholarship eligibility is $90,696 ($49,025 X 185%). To qualify for a STO scholarship, a student must meet one of the following criteria:

- Was homeschooled or attended public school in the prior school year.
- Moved to Arizona from another state before enrolling in a qualified school.
- Participated in an Arizona Empowerment Scholarship Account (ESA) without accepting or renewing the scholarship.
- Entering kindergarten in the upcoming school year.
- Received tuition assistance from a STO during the prior school year.

The maximum scholarship amounts for 2021 are $5,600 for grades K-8 and $7,500 for grades 9-12. Those amounts increase by $200 annually pursuant to A.R.S. § 43-1504C. Lastly, a corporation may not use a tax credit for any contribution if a corporation designates the scholarship for a particular student.

Refundable

The credit is not refundable.

Carry Forward

The unused portion of the credit may be carried forward for a maximum of 5 consecutive years.

Transferable

The credit is not transferable.

History and Rationale

The C-Corp STO "low-income scholarship" tax credit was created by Laws 2006, Chapter 14 and became effective starting in FY 2007. The purpose of the program is to encourage corporate contributions to STOs that award "low-income scholarships" that enable students to attend non-governmental elementary and secondary schools.

As originally enacted, total corporate tax credits to STOs for "low-income scholarships" was capped at $5 million and included a sunset date of June 30, 2011. Laws 2006, Chapter 325 raised the cap to $10 million and by an additional 20% annually, beginning in FY 2008.

In September 2006, the Arizona School Boards Association and the Arizona Chapter of the American Civil Liberties Union filed suit against the state regarding this tax credit. In *Green v. Garriott*, plaintiffs alleged that corporate contribution "set asides" in the associated laws violated the "general and uniform" provision of the state's public education system. The Maricopa County Superior Court ruled in favor of the state in a ruling that was later upheld by the Arizona Court of Appeals. The plaintiffs appealed to the Arizona Supreme Court, but in 2009 it declined to review the case, making the Maricopa County Superior Court ruling stand.

Laws 2009, Chapter 168 expanded the credit by making it available to insurers and repealed the June 30, 2011 sunset date. Laws 2015, Chapter 301 expanded the credit to include businesses classified as Subchapter S corporations. Laws 2019, Chapter 281 limits the annual increase of the credit cap to 15% in FY 2021, 10% in FY 2022, and 5% in FY 2023. Beginning in FY 2024, the increase of the credit cap is limited to the greater of 2% or the annual change of the Metropolitan Phoenix consumer price index. In dollar terms, Chapter 281 limits the credit to $123.0 million in FY 2021, $135.3 million in FY 2022, and $142.1 million in FY 2023.

Revenue Impact

Relative to their shared statutory limitation, *Table 1* summarizes C-Corp, S-Corp, and insurer contributions to STOs for "low-income scholarships" since FY 2007. In most years, DOR approves the use of credits at or near the cap level. Taxpayers, however, may not fully claim their available credit in the year approved and may carry it forward for 5 years.

Table 1

Corporate Contributions to School tuition Organizations for "Low-Income Scholarships"

Fiscal Year [1/]	Statutory Limitation [2/]	# of Corporations [3/]	$ Approved by DOR
2007	$10,000,000	108	$9,740,800
2008	$12,000,000	73	$12,116,000
2009	$14,400,000	98	$10,816,006
2010	$17,280,000	60	$8,121,508
2011	$20,736,000	68	$11,365,351
2012	$24,883,200	83	$19,587,037
2013	$29,859,840	114	$30,041,114
2014	$35,831,808	99	$36,571,808
2015	$42,998,170	95	$42,997,170
2016	$51,597,804	203	$51,597,804
2017	$61,917,365	371	$61,917,164
2018	$74,300,838	662	$74,300,838
2019	$89,161,006	704	$89,161,006
2020	$106,993,207	880	$106,983,528
2021	$123,042,188	N/A [4/]	$122,717,188
2022	$135,346,407	N/A [4/]	$112,014,130 [5/]
2023	$142,113,727	N/A [4/]	N/A [4/]

1/ DOR reports contributions on a fiscal year rather than tax year basis, since the statutory limitation on such contributions in A.R.S. § 43- 1183C is per fiscal year. DOR, however, reports corresponding tax credit data on a tax year basis.

2/ Increased 20% annually through FY 2020. Laws 2019, Chapter 281 limits the increase to 15% in FY 2021, 10% in FY 2022, and 5% in FY 2023.

3/ Includes insurers starting in FY 2010 and S Corporations starting in FY 2016.

4/ DOR has not reported these amounts as of publication.

5/ This amount is preliminary midway through the fiscal year.

Table 2 includes 6 fiscal years of data on credit use for C corporations, S corporations, and insurers. During those years, C-Corp usage has declined while S-Corp and insurer usage has increased significantly.

Table 2

Low-Income STO Tax Credit Use by Fiscal Year

Fiscal Year	# of C-Corp Claimants	C-Corp Credit Used	# of S-Corp Claimants	S-Corp Credit Used	Insurers' Credit Used*	Total Credit Used
2016	71	$28,065,303	73	$967,990	$22,786,396	$51,819,689
2017	76	$21,849,744	145	$1,344,614	$23,246,639	$46,440,997
2018	98	$32,977,938	354	$4,411,353	$30,785,353	$68,174,644
2019	98	$18,282,920	637	$16,616,451	$26,910,421	$61,809,792
2020	97	$22,465,054	855	$31,461,005	$45,419,852	$99,345,911
2021	114	$20,058,461	918	$29,258,009	$46,610,732	$95,927,202

# of Claimants- the number of taxpayers who claimed the credit

Credit Used- the total value of credits claimed

* The Department of Insurance and Financial Institutions does not report the number of claimants for the insurer portion of the credit

The tax credit may impact state K-12 education costs because some students receiving the scholarships may have otherwise enrolled in public schools if the scholarship had not been available. Currently each pupil added to the statewide K-12 Average Daily Membership (ADM) count costs the state General Fund on average about $7,200. Each pupil switching to a private school in response to the availability of the STO scholarship could therefore generate a corresponding General Fund Basic State Aid savings of $(7,200). The total magnitude of the K-12 savings, however, is unknown because the number of students who decide to attend private school based primarily on the availability of the STO scholarship is unknown.

Economic Benefits

This credit is not directly designed to promote economic development or spur new investments that would result in new jobs. Instead, according to DOR's August 2000 report "Income Tax Credits in Arizona," this credit is one of several tax credits in statutes primarily intended to encourage cash contributions to certain target groups in society, such as the working poor or students in private or public schools.

In FY 2020, STOs distributed $87.3 million in scholarships (29,829 scholarships to 281 schools) from C-Corps, S-Corps, and insurance premium tax "low-income scholarship" contributions (last available data, see *Table 3* below). The average "low-income" scholarship was $2,928. Individual students may receive scholarships from more than one STO.

Between FY 2007 and FY 2020, the number of low-income scholarships grew from 1,940 to 29,829. At the same time, the total amount of dollars distributed grew from $4.6 million to $87.3 million.

Complexity

According to DOR, it is administratively simple for corporations to donate to STOs and claim the tax credit, but administratively complicated for the STOs to request pre-approval and for DOR to process the applications. DOR believes that a majority of STOs are not staffed by full-time employees, which can add to the difficulty of preparing the reporting requirements. DOR reviews the annual reports and verifies statutory compliance for all STOs, which is a lengthy process due to the number of STOs.

Potential Performance Measures

Performance measures could include:

1. Percentage of STO revenues retained for administrative costs.

   The STOs would have this information readily available.

2. The amount of STO scholarship money spent per student.

   This information appears to be collected by STOs but would require additional reporting.

Prior Review

The credit was last reviewed in 2016. However, since the Joint Legislative Income Tax Credit Review Committee did not meet that year, no recommendations were made by the Committee. When the credit was reviewed in 2011, the Committee recommended that the credit be continued.

Table 3

FY 2020 Low-Income Scholarships by School Tuition Organization

	# of Recipients	Total Scholarships	Average Scholarship
AAA Scholarship Foundation	2,386	$11,959,912	$5,013
Academic Opportunity of Arizona	17	73,359	4,315
Arizona's Scholarship Konnection Inc.	210	607,923	2,895
Arizona Education and Scholarship Opportunity Program	550	1,507,212	2,740
Arizona Education First	2	11,000	5,500
Arizona Education Scholarship Foundation	258	94,630	367
Arizona Episcopal Schools Foundation	114	563,257	4,941
Arizona Independent Schools Scholarship Foundation	150	914,805	6,099
Arizona International Academy Scholarship Fund	12	31,500	2,625
Arizona Leadership Foundation	6,548	30,216,697	4,615
Arizona Lutheran Scholarship Organization	120	73,435	612
Arizona Private Education Scholarship Fund Inc	906	2,366,902	2,612
Arizona Private School Tuition Organization	224	203,248	907
Arizona School Choice Trust	482	1,384,631	2,873
Arizona Tax Credit	224	384,852	1,718
Arizona Tuition Connection	1,958	5,552,928	2,836
Arizona Tuition Organization	141	67,519	479
Arizona Waldorf Scholarship Foundation	92	98,383	1,069
Arizona's Catholic Tuition Support Organization (CTSO)	2,006	3,950,371	1,969
Best Student Fund	70	243,300	3,476
Brophy Community Foundation	2,569	6,056,382	2,357
Catholic Education Arizona	3,599	5,880,280	1,634
Chabad Tuition Organization	69	337,500	4,891
Christ Lutheran School Tuition Organization	38	28,139	741
Christian Scholarship Fund of Arizona	11	29,212	2,656
Cochise Christian School Tuition Organization	25	7,003	280
Community Tuition Grant Organization, Inc	162	240,250	1,483
Corporate Tax Foundation	137	702,098	5,125
Financial Assistance for Independent Schools	32	182,176	5,693
Greater Arizona, Inc.	100	413,444	4,134
Independent Schools Corporate Tax Foundation	220	884,586	4,021
Institute for Better Education (IBE)	1,649	1,533,583	930
Jewish Education Tax Credit Organization (JETCO)	59	189,050	3,204
Jewish Tuition Organization	247	1,098,963	4,449
Montessori Scholarship Organization	26	72,510	2,789
Northern Arizona Christian School Scholarship Fund	79	49,639	628
Pappas Kids Schoolhouse Foundation	683	1,453,338	2,128
Private School Tuition Fund 123	72	104,177	1,447
School Choice Arizona, Inc.	1,700	4,346,951	2,557
School Tuition Association of Yuma	617	1,580,647	2,562
School Tuition Organization 4 Kidz	224	256,109	1,143
Students First Foundation	89	70,708	794
Tuition Organization for Private Schools	769	978,299	1,272
Valley Tuition Organization	117	461,200	3,942
White Mountain Tuition Support Foundation	18	31,336	1,741
Yuma's Education Scholarship Fund for Kids	48	45,089	939
TOTAL	**29,829**	**$87,338,533**	**$2,928**

Attachment B

Corporate Contributions to School Tuition Organizations for Displaced or Disabled Pupils

Summary

- The credit is capped at $6.0 million annually.
- The cost of the credit was $7.9 million in FY 2024 ($2.2 million for corporations, $5.4 million for insurers, and $0.3 million for individuals (S-corporations)). Depending on the tax year in which the taxpayer claims the credit, the amount on a fiscal year basis can exceed the $6 million cap.
- In FY 2024, the credit was claimed by 22 individuals (S-corporations) at an average of $13,593 per claim, and by 9 corporations at an average of $238,870 per claim.
- In total, there are 4 private school tax credits with a combined cost of $234.7 million for FY 2024.

Statute

A.R.S. § 43-1184, A.R.S. § 43-1089.04, and § 20-224.07

Description

The credit was last reviewed in 2019. The description of the credit as well as other sections of the credit review have been updated from our 2019 report when relevant.

Current law authorizes tax credits for 4 different types of contributions to school tuition organizations (STOs):

1. Corporate, individual (S-corporation), and insurer contributions to STOs awarding "low-income scholarships" (A.R.S § 43-1183, § 43-1089.04 and § 20-224.06),
2. Corporate, individual (S-corporation), and insurer contributions to STOs awarding "displaced or disabled pupil scholarships" (A.R.S § 43-1184, § 43-1089.04 and § 20-224.07),
3. Private contributions by individuals to STOs awarding scholarships to private school students. (This credit is commonly referred to as the "Original STO Credit" A.R.S § 43-1089, A.R.S § 43-1601 through § 43-1605), and
4. Private contributions by individuals to STOs awarding "switcher scholarships" to students switching from one mode of school to private school if the amount of the taxpayer's donation exceeds the "Original STO Credit" limit under A.R.S § 43-1089. (This credit is commonly referred to as the "Switcher STO Credit" A.R.S § 43-1089.03, A.R.S § 43-1601 through § 43-1605).

This review pertains to corporate income tax credits for displaced or disabled pupil scholarship contributions pursuant to A.R.S § 43-1184. It also addresses individual (S-corporation) income tax credits and insurance premium tax credits for displaced or disabled pupil scholarship contributions pursuant to A.R.S § 43-1089.04 and A.R.S § 20-224.07, respectively. Individuals (as shareholders of an S corporation) and insurers share the program's $6 million annual tax credit cap. The tax credit review statute (A.R.S. § 43-222), however, does not literally require review of individual (S-corporation) income tax credits and insurance premium tax credits for "displaced or disabled" STO contributions.

This credit is provided to corporations, individuals (as shareholders of an S-corporation), and insurers for voluntary contributions to STOs. A STO is a charitable organization that is exempt from federal taxation and that allocates at least 90% of its revenue for educational scholarships or tuition grants to children to attend non-governmental elementary or secondary schools. A STO may use up to 10% of corporate contributions for administration expenses.

STO scholarships from this program may be awarded only to students who lived in foster care at any time prior to graduating from high school or obtaining a GED, or who have been identified at any time as having a disability under federal or state law. Prior to FY 2015, recipients typically also had to be prior public school pupils, but that restriction and other related qualifiers (such as being a military dependent) were eliminated by Laws 2014, Chapter 278.

A student's scholarship or grant under the program is capped at the actual cost of their tuition or at 90% of the amount of state aid that the student would receive if in public school, whichever is less (A.R.S. § 43-1505B). A corporation, S-corporation, or insurer may not use a tax credit for any contribution for displaced or disabled pupil scholarships if it designates the contribution for a particular student.

The Arizona Department of Revenue (ADOR) typically reports tax credit data for this program separately from related data on STO contributions and scholarships, and typically reports more current data for the former. In addition, some of ADOR's tax credit data excludes insurers, and the Arizona Department of Insurance and Financial Institutions (DIFI) reports less detailed data on insurer tax credits for the program than ADOR reports for corporations and S-corporations. This analysis uses whatever available data are most recent and complete for each metric. This analysis is therefore not always able to compare data for different program metrics, such as STO contributions and tax credits claimed, for the same fiscal year.

Refundable

The credit is not refundable.

Carry Forward

The unused portion of the credit may be carried forward for a maximum of 5 consecutive years.

History and Rationale

The corporate and insurer displaced or disabled pupil scholarship tax credits were both created by Laws 2009, 2nd Special Session, Chapter 1 and became effective starting in FY 2010. They were established after the Arizona Supreme Court ruled in March 2009 that prior scholarship programs established for displaced or disabled pupils by Laws 2006, Chapters 340 and 358 violated a prohibition in the state Constitution on appropriating public monies to private schools. The displaced or disabled pupil scholarship tax credit program addressed that ruling by funding scholarships for displaced or disabled pupils indirectly through tax credit-eligible STO contributions from corporations and insurers, rather than directly from the state General Fund.

In September 2006 (3 years before the displaced or disabled pupil scholarship tax credits took effect), the Arizona School Boards Association and the Arizona Chapter of the American Civil Liberties Union filed suit against the state regarding the related corporate "low-income student scholarship" STO tax credit (A.R.S § 43-1183). In *Green v. Garriott*, plaintiffs alleged that corporate contribution "set asides" in the associated laws violated the "general and uniform" provision of the state's public education system. The Maricopa County Superior Court ruled in favor of the state in a ruling that was later upheld by the Arizona Court of Appeals. The plaintiffs appealed to the Arizona Supreme Court, but in 2009 it declined to review the case, making the Superior Court ruling stand.

Laws 2015, Chapter 301 expanded the credit for displaced or disabled pupil scholarship contributions to include businesses classified as Subchapter S corporations. (Chapter 301 allows an individual shareholder to claim the credit for their pro rata share of the contributions by an S Corporation to a STO.)

Corporations, individuals (S-corporations), and insurers also may receive tax credits for contributions to STOs under a separately authorized program for "low-income" students. The "low-income pupil scholarship" STO tax credit is not subject to Committee review this year. *Attachment 1* provides an overview of all current STO tax credit programs.

The statute creating the displaced or disabled pupil scholarship income tax credit program does not include a specific statement of purpose or a rationale. As noted above, however, the program was created after a related state-funded program for providing scholarships to displaced or disabled students was ruled unconstitutional.

Revenue Impact

There is no separate cap on the amount of tax credits that an individual corporation, individual (S-corporation), or insurer can claim under the program. However, from FY 2010 (the inception of the credit) to FY 2021, the aggregate corporate, individual (S-corporation), and insurer tax credits for contributions for displaced or disabled pupil scholarships were capped at \$5.0 million per year. Laws 2021, Chapter 412 increased the cap to \$6.0 million per year, beginning in FY 2022. Because of this cap, STO contributions from corporations, individuals (S-corporations), and insurers must be pre-approved by the ADOR to be eligible for a tax credit. Since FY 2015, contributions from corporations, individuals (S-corporations) and insurers combined have met the annual cap (*see Table 1 below*).

Table 1 summarizes contributions to STOs for displaced or disabled pupil scholarships since the beginning of the program in FY 2010 through FY 2023 (data for FY 2024 will not be released until the spring of 2025). In FY 2023 (latest published data on donations received), 18 individuals (S-corporations) and 3 insurers (21 donors total) donated a total of \$6.0 million to STOs under the program. The average contribution made by donors in the first year of the program (FY 2010) was \$246,500 (\$1,478,880 ÷ 6 corporations). The average contribution in the most recent year for which data is available (FY 2023) was \$285,700 (\$6,000,000 ÷ 21 donors).

ADOR also reports tax credits claimed for STO contributions on a tax year basis. Every taxpayer is required to calculate their taxable income based on an annual accounting period called a tax year. For most individual income taxpayers, the calendar year is also their tax year. Other taxpayers, such as regular corporations and S corporations may use a fiscal year as their tax year. A corporation's fiscal year is 12 consecutive months ending on the last day of any month except December 31. Depending on a corporation's elected tax year (calendar year or fiscal year) and whether the corporation files for a 6-month extension, the corporation's liability for any one tax year could affect collections in 1 of 4 state fiscal years.

Table 1

Contributions to School Tuition Organizations for Displaced or Disabled Pupil Scholarships by Fiscal Year [1/]

Fiscal Year	Statutory Limitation	# of Donors	$ Approved by DOR [2/]	$ Received by STOs
2010	$5,000,000	6	$1,478,880	$1,478,880
2011	$5,000,000	8	$1,079,000	$1,029,000
2012	$5,000,000	6	$283,000	$283,000
2013	$5,000,000	14	$3,580,350	$3,505,350
2014	$5,000,000	27	$3,112,745	$2,957,765
2015	$5,000,000	28	$5,000,000	$5,000,000
2016	$5,000,000	38	$5,325,000	$5,000,000
2017	$5,000,000	34	$5,147,000	$5,000,000
2018	$5,000,000	14	$5,000,000	$5,000,000
2019	$5,000,000	50	$5,000,000	$5,000,000
2020	$5,000,000	42	$5,973,400	$5,000,000
2021	$5,000,000	29	$7,700,500	$5,000,000
2022	$6,000,000	20	$6,050,000	$6,000,000
2023	$6,000,000	21	$6,321,000	$6,000,000
2024	$6,000,000	NA	NA	NA

1/ Data are for corporations, individuals (S-corporations) and insurers combined.

2/ After approval by DOR, a taxpayer must make its donation to the STO within 20 days (A.R.S § 43-1184D). If a taxpayer fails to meet the required 20-day donation window, the taxpayer's approved credit amount is forfeited. The column "Approved by DOR" reflects the amount of credits that DOR approved within a fiscal year regardless of whether the taxpayer made the donation within the required 20-day window.

Source: "School Tuition Organization Income Tax Credits in Arizona: Fiscal Year 2023" (page 39) from the Arizona Department of Revenue (March 2024)

Table 2 summarizes tax credit claims for corporations and individuals (S-corporations) for the program by tax year since its inception, as reported by ADOR. TY 2022 data for individuals (S-corporations) are preliminary due to extension returns pending at the time of the report. Note that this information does not include credit claims by insurers.

Contributions do not necessarily result in the taxpayer using the credit immediately. A corporation, individual (S-corporation), or insurer may lack enough liability to take the full credit in the year in which the donation is made. To address that issue, A.R.S. § 43-1184E, A.R.S. § 43-1098.04C, and A.R.S. § 20-224.07D allow them to carry forward any claimed but unused credit for up to 5 years. *Table 2* shows the amount of credits claimed and carried forward by corporations and individuals (S-corporations) by tax year since the program's inception. Similar but less detailed data for insurers are summarized in *Table 3*.

Table 2

Tax Credit Claims by Tax Year (Corporations and S-corporations only) [1/] [2/]

Tax Year	# of Claimants [3/]	Total Credit Available [4/]	Credits Used [5/]	Carry-Forward
2009	1	NR	NR	NR
2010	1	NR	NR	NR
2011	3	$170,000	$170,000	$0
2012	4	NR	NR	NR
2013	14	$506,600	$368,600	$138,000
2014	17	$2,624,300	$2,334,000	$290,300
2015	29	$2,684,200	$2,388,400	$601,600
2016	21	$1,190,400	$769,100	$421,200
2017 [6/]	35	$380,700	$318,500	$62,200
2018	47	$2,215,500	$2,007,200	$208,300
2019	40	$1,532,000	$1,245,000	$287,000
2020 [6/]	33	$646,300	$422,900	$223,400
2021 [7/]	33	$1,667,200	$1,151,700	$441,600
2022 [8/]	28	$1,243,800	$970,600	$29,700

1/ As reported by the Arizona Department of Revenue (ADOR). Excludes credits claimed by insurers, which are not reported by ADOR. The Arizona Department of Insurance and Financial Institutions (DIFI) reports tax credit usage data for insurers for this program, but in a less detailed manner and on a fiscal year rather than tax year basis *(see Table 3).*

2/ The table combines data reported for corporations and individuals (S-corporations).

3/ The number of taxpayers who claimed the credit in each year.

4/ The total tax credits identified in each tax year, including any new credits and any credits carried over from a previous year and identified in that year.

5/ The total value of credits claimed in each tax year.

6/ No data publicly released by ADOR for Corporate Credits in TY 2017 and TY 2020. Amounts of credit available, credits used, and credit carry-forward in TY 2017 and TY 2020 are solely for individual income taxpayers (S-corporations).

7/ The amount of credit carry-forward for TY 2021 is solely for individual income taxpayers (S-corporations).

8/ The amount of credit carry-forward for TY 2022 is solely for individual income taxpayers (S-corporations). Corporate credit use is preliminary for TY 2022.

NR – Data is not releasable due to Arizona confidentiality laws.

Source: Arizona Department of Revenue "Arizona's Individual and Corporate Income Tax Credit Report (November 2023)."

Table 3 below summarizes tax credit data for insurance companies by fiscal year, as reported by DIFI. This data is available from FY 2015 through FY 2024. *Table 3* does not include any information on the number of claims, as such data is not reported by DIFI.

Given the multi-year period over which corporations and insurers can claim credits under this program, the *Table 1* data on contributions are probably more reflective of the credit's current use than the *Table 2* & *3* data on credit usage.

The credit may result in foregone General Fund spending to the extent that STO-funded scholarships result in reduced public school enrollment. We are unable, however, to determine whether or how many additional students would have attended public schools instead of private schools without a STO scholarship.

Table 3
Tax Credit Claims by Fiscal Year (Insurers only) 1/

Fiscal Year	Credit Used
2015	$2,988,400
2016	$2,950,900
2017	$3,477,300
2018	$2,762,900
2019	$3,448,100
2020	$2,949,100
2021	$4,325,700
2022	$5,589,500
2023	$5,602,200
2024	$5,443,400

1/ As reported by the Arizona Department of Insurance and Financial Institutions (DIFI). DIFI was not required to report this information prior to FY 2015.

Economic Benefits

This credit is not directly designed to promote economic development or spur investments that would result in new jobs. Instead, this credit is one of several tax credits in statute that appears to be primarily intended to encourage cash contributions to certain target groups in society, such as the working poor or students in private or public schools.

More Background

In FY 2023 (latest published data), STOs distributed $4,490,197 in displaced or disabled pupil scholarships (1,168 scholarships to 137 schools) from individual (S-corporation) and insurer contributions (*see Table 4*). In addition, STOs sometimes dedicate a portion of current year donations for multi-year scholarships for specific students, rather than earmarking all prior year contributions for current year scholarships. The data cited in *Table 4* are from STO annual reports, rather than corporate or insurer income tax filings, so are not confidential.

In FY 2023 (latest published data), STOs distributed $4,490,197 in displaced or disabled pupil scholarships (1,168 scholarships to 137 schools) from individual (S-corporation) and insurer contributions (*see Table 4*). In addition, STOs sometimes dedicate a portion of current year donations for multi-year scholarships for specific students, rather than earmarking all prior year contributions for current year scholarships. The data cited in *Table 4* are from STO annual reports, rather than corporate or insurer income tax filings, so are not confidential.

Historically, the average displaced or disabled pupil scholarship has varied from a low of $3,360 in FY 2013 to a high of $5,485 in CY 2009 (the program's first year) *(see Table 5).* The number of scholarships distributed under the program has remained relatively stable since FY 2017.

ADOR's March 2024 STO report notes that the number of scholarships paid does not equate to the number of students receiving scholarships because families often apply for scholarships from more than one STO. Thus, the number of scholarships reported in *Tables 4* and *5* do not equal the number of students receiving STO scholarships from this program. Schools do not report the number of individual students receiving STO scholarships.

Table 4

Displaced or Disabled Pupil Scholarships for Fiscal Year 2023 by School Tuition Organization

School Tuition Organization	# of Scholarships	# of Schools	Scholarship Amount	Average
Academic Opportunity of Arizona	46	15	$453,297	$9,854
America's Scholarship Konnection Inc.	5	1	$24,000	$4,800
Arizona Leadership Foundation	432	82	$2,774,121	$6,422
Arizona Private Education Scholarship Fund, Inc.	75	15	$296,755	$3,957
Arizona School Choice Trust	1	1	$2,503	$2,503
Arizona Tuition Connection	3	2	$6,500	$2,167
Arizona's Catholic Tuition Support Organization (CTSO)	21	8	$38,415	$1,829
Catholic Education Arizona	151	32	444,793	$2,946
Financial Assistance for Independent Schools	18	1	$120,391	$6,688
Institute for Better Education	380	103	$229,971	$605
School Choice Arizona, Inc.	36	12	$99,451	$2,763
TOTAL	**1,168**	**137** 1/	**$4,490,197**	**$3,844**

1/ Unduplicated total, as some schools received scholarships from more than one STO.
Source: "School Tuition Organization Income Tax Credits in Arizona: Fiscal Year 2023" (page 44) from the Arizona Department of Revenue (March 2024)

Table 5

Displaced or Disabled Scholarships by Fiscal Year

Fiscal Year	# STOs	# Scholarships	$ Distributed	Avg. Scholarship
2009 1/	5	114	$625,335	$5,485
2010 1/	6	166	$715,424	$4,310
2011	5	114	$559,333	$4,906
2012	5	119	$583,865	$4,906
2013	6	217	$731,231	$3,360
2014	8	346	$1,611,469	$4,657
2015	12	806	$3,581,873	$4,444
2016	14	934	$4,370,439	$4,679
2017	18	1,103	$5,750,839	$5,214
2018	14	1,162	$5,205,607	$4,480
2019	14	1,105	$5,860,589	$5,304
2020	11	961	$4,885,395	$5,084
2021	15	928	$4,518,492	$4,869
2022	13	1,345	$5,061,161	$3,763
2023	11	1,168	$4,490,197	$3,844

1/ Reported data are for calendar year rather than fiscal year (reporting period changed after FY 2010).

Source: "School Tuition Organization Income Tax Credits in Arizona: Fiscal Year 2023" (page 41) from the Arizona Department of Revenue (March 2024)

There are 4 different private school STO tax credit programs *(see Attachment 1).* Students received 75,817 scholarships from the 4 STO scholarship programs combined in FY 2023 *(see Table 6)*. Some pupils, such as public school switchers and military dependents, can receive scholarships from more than one STO program (such as Switcher and Corporate Low Income) in addition to receiving scholarships from more than one STO within the same STO program (such as Switcher).

Table 6

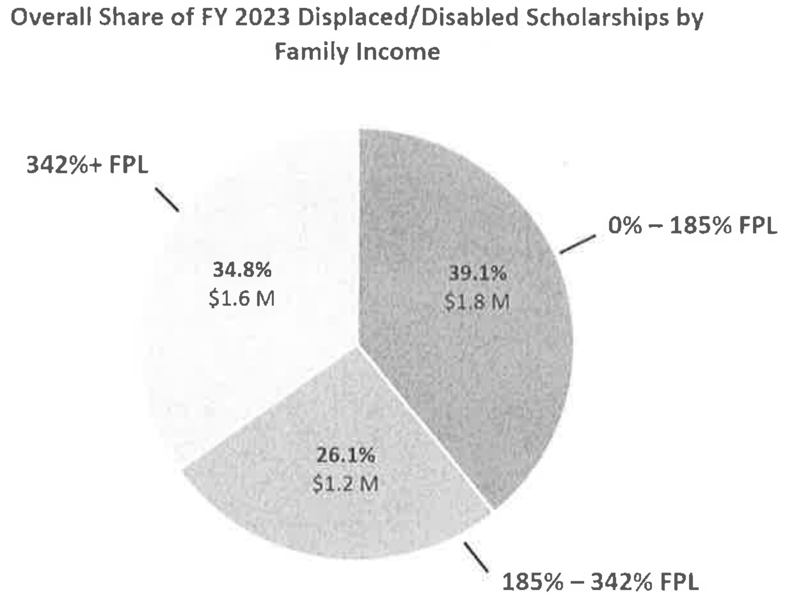
Scholarship Summary for All STO Program Combined for FY 2023

STO Program	Number of Scholarships	Scholarships ($)	Tax Donations ($)
Original Individual	23,826	$49,878,260	$69,544,712
Switcher Individual	21,241	$36,322,839	$46,695,361
Low-Income Corporate	29,582	$113,411,370	$142,111,227
Displaced/Disabled Corporate	1,168	$4,490,197	$6,000,000
Total	**75,817**	**$204,102,666**	**$264,351,300**

Source: " School Tuition Organization Income Tax Credits in Arizona: Fiscal Year 2023" (pages 11, 21, 30, and 39) from the Arizona Department of Revenue (March 2024)

A.R.S. § 43-1603B5 requires STOs to report the percentage and total dollar amount of scholarships awarded during the previous year to the following: 1) students whose family income qualifies them for free or reduced price lunches (FRPL) under the federal school lunch program (up to 185% of the poverty level, or $51,337 for a family of four for FY 2023), and 2) students whose family income exceeds the FRPL eligibility threshold by less than 185% (up to 342.25% of the poverty level, or $94,974 for a family of 4 for FY 2023). ADOR reports that for FY 2023, students with family income of up to 185% of the federal poverty level (FPL) received 39.1% ($1.8 million) of program scholarships that year and that students with family income of 185% to 342% of the FPL received 26.1% ($1.2 million) of scholarships. The remaining 34.8% of scholarships ($1.6 million) went to students whose family income was greater than 342% of the FPL ($94,974 for a family of 4 for FY 2023) (see *Chart 1*).

Chart 1



Complexity

ADOR indicates that it is administratively simple for corporations, insurers, and individuals (S-corporations) to donate to STOs and claim the credit. However, the large volume of corporate donation pre-approval requests and the statutory requirement to process them on a first-come/first-served basis requires a process that is complex for both the STOs and ADOR. According to ADOR, recent process improvements have increased the efficiency of credit pre-approval for both STOs and ADOR.

ADOR continues to use a streamlined annual reporting process for the STOs. ADOR reports, however, that many STOs still utilize volunteer staff, which leads to reporting inconsistencies and makes it difficult to educate STO staff on reporting requirements. ADOR indicates that its oversight responsibilities of STOs currently rely on the review of annual reports and audits/reviews submitted by the STOs. It notes that oversight by ADOR could be enhanced with additional staffing capacity.

Potential Performance Measures

Performance measures could include:

1. Percentage of STO revenues retained for administrative costs.

   The STOs would have this information readily available.

2. Percentage of private school tuition paid for with award funding.

   This information appears to be collected by STOs but would require additional reporting.

Prior Review

Attachment B

The Credit for Contributions to School Tuition Organizations for Displaced or Disabled Students was previously reviewed during the 2019 review cycle. The Committee recommended that the credit be retained and placed on the income tax credit review schedule for 2024.