

**DESCRIPTION OF H.R. 9462, THE
“EDUCATIONAL CHOICE FOR CHILDREN ACT OF 2024”**

Scheduled for Markup
by the
HOUSE COMMITTEE ON WAYS AND MEANS
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Prepared by the Staff
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INTRODUCTION

The House Committee on Ways and Means has scheduled a committee markup for September 11, 2024, of H.R. 9462, the “Educational Choice for Children Act of 2024.” This document,¹ prepared by the staff of the Joint Committee on Taxation, provides a description of this bill.

¹ This document may be cited as follows: Joint Committee on Taxation, *Description of H.R. 9462, the “Educational Choice for Children Act of 2024”* (JCX-41-24), September 9, 2024. This document can also be found on the Joint Committee on Taxation website at www.jct.gov. All section references in the document are to the Internal Revenue Code of 1986, as amended (the “Code”), unless otherwise stated.

**A. Tax Credit for Contributions of Individuals to Scholarship Granting Organizations;
Exemption from Gross Income for Scholarships for Qualified
Elementary or Secondary Education Expenses of Eligible Students;
Organizational and Parental Autonomy**

Present Law

Charitable contribution deduction

In computing taxable income, an individual taxpayer who itemizes deductions or a corporate taxpayer generally is allowed to deduct the amount of cash and the fair market value of property contributed to an organization described in section 501(c)(3) or to a Federal, State, or local governmental entity, including to most educational organizations.²

The amount of the deduction allowable for a taxable year with respect to a charitable contribution of property may be reduced depending on the type of property contributed, the type of charitable organization to which the property is contributed, and the income of the taxpayer.³ For individual taxpayers, the income-based limitation on the charitable contribution deduction is higher for gifts made to public charities than for gifts made to private foundations. Contributions of cash to a public charity generally are deductible up to 60 percent⁴ of the donor's adjusted gross income ("AGI")⁵ (30 percent for capital gain property, and 50 percent for non-capital gain property other than cash), whereas contributions to most private foundations generally are deductible up to 30 percent of the donor's AGI (20 percent for capital gain property).⁶ For corporate taxpayers, the deductible amount of charitable contributions generally is limited to 10 percent of taxable income.⁷ For all taxpayers, gifts of capital gain property to a public charity generally are deductible at the property's fair market value,⁸ whereas gifts of capital gain

² Within certain limitations, donors also are entitled to deduct such contributions for estate and gift tax purposes. See secs. 2055 and 2522.

³ Sec. 170(b) and (e).

⁴ For contributions made in taxable years beginning after December 31, 2025, the 60-percent limit is reduced to 50 percent. Sec. 170(b)(1)(G)(i).

⁵ The charitable percentage limits are applied to the donor's "contribution base," which is the donor's AGI computed without regard to any net operating loss carryback to the taxable year under section 172. Sec. 170(b)(1)(H).

⁶ Sec. 170(b)(1).

⁷ Sec. 170(b)(2).

⁸ Sec. 170(e)(1). However, contributions of tangible personal property not for an exempt purpose of the donee organization are deductible at the taxpayer's basis in the property. Sec. 170(e)(1)(B)(i). A special rule determines the aggregate deduction for contributions of certain intellectual property. Sec. 170(e)(1)(B)(iii) and 170(m).

property (other than publicly traded stock) to most private foundations are deductible at the taxpayer's basis (cost) in the property.⁹

Qualified scholarships and qualified tuition reduction

Present law provides an exclusion from gross income for income tax purposes and from wages for employment tax purposes for amounts received as a qualified scholarship by an individual who is a candidate for a degree at an educational organization described in section 170(b)(1)(A)(ii) (a "qualifying educational organization").¹⁰ In general, a qualified scholarship is any amount received by such an individual as a scholarship or fellowship grant if the amount is used for qualified tuition and related expenses. Qualified tuition and related expenses include tuition and fees required for enrollment or attendance, or for fees, books, supplies, and equipment required for courses of instruction, at the qualifying educational organization. This definition does not include regular living expenses, such as room and board. A qualifying educational organization is an educational organization that normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on. These institutions include K-12 schools.

Present law also provides an exclusion from gross income for income tax purposes and from wages for employment tax purposes for qualified tuition reductions for certain education (below the graduate level) that is provided to employees (and their spouses and dependents) of qualifying educational organizations.¹¹ The education must be provided at the employing organization or another qualifying educational organization. This exclusion does not apply to any amount received by a student that represents payment for teaching, research, or other services by the student required as a condition for receiving the tuition reduction.

Gift tax exclusion for educational expenses

Under present law, gift tax is imposed on transfers of property by gift, subject to several exceptions. One exception is the gift tax annual exclusion of section 2503(b). Under this exclusion, a donor can transfer up to \$18,000 of property to each of an unlimited number of donees without incurring gift tax on such transfers.¹²

In addition to the gift tax annual exclusion, the Code provides that certain tuition payments are not considered transfers of property by gift for gift tax purposes.¹³ This exclusion covers amounts paid on behalf of an individual as tuition to a qualifying educational

⁹ Sec. 170(e)(1)(B)(ii) and 170(e)(5).

¹⁰ Secs. 117(a) and 3121(a)(20).

¹¹ Secs. 117(d) and 3121(a)(20).

¹² The Code provides an amount of \$10,000 for the maximum gift tax annual exclusion, adjusted in \$1,000 increments for inflation occurring after 1997. The inflation-adjusted amount for 2024 is \$18,000.

¹³ Sec. 2503(e).

organization. An unlimited exclusion applies only to direct transfers to the educational institution, not to reimbursements to donees for amounts paid by them for otherwise qualifying services, or to trusts to provide for the education of designated beneficiaries.¹⁴ Further, an unlimited exclusion is not permitted for books, supplies, dormitory fees, board, or other similar expenses that do not constitute direct tuition costs.¹⁵ This exclusion applies without regard to the relationship of the donor and donee.

Description of Proposal

Tax credit for contributions of individuals to scholarship granting organizations

Individual income tax credit

The proposal creates a nonrefundable income tax credit that is equal to the aggregate amount of qualified contributions made by the taxpayer during the taxable year. The credit allowed to a taxpayer for a taxable year may not exceed the greater of 10 percent of the taxpayer's aggregate gross income or \$5,000. An individual is allowed the credit only to the extent that the Secretary of the Treasury (the "Secretary"), subject to an aggregate volume cap that is described below, allocates the credit to the individual.

For purposes of the credit, a "qualified contribution" is a charitable contribution (within the meaning of section 170(c)) to a scholarship granting organization in the form of cash or marketable securities. The amount allowed as a credit to a taxpayer for a taxable year is reduced by the amount allowed as a credit on any State tax return of the taxpayer for qualified contributions made by the taxpayer during the taxable year. The proposal provides that any qualified contribution for which a credit is allowed is not taken into account as a charitable contribution for purposes of section 170.

A "scholarship granting organization" is any organization (a) that is described in section 501(c)(3), is exempt from tax under section 501(a), and is not a private foundation; (b) substantially all of the activities of which are providing scholarships for qualified elementary or secondary education expenses of eligible students; (c) that prevents the co-mingling of qualified contributions with other amounts by maintaining one or more separate accounts exclusively for qualified contributions; and (d) that either meets the requirements to be a scholarship granting organization (discussed below) or was eligible on the date of enactment to receive contributions for which the donor is entitled to a State tax credit if the contributions are used by the organization to provide scholarships. An "eligible student" is an individual who is a member of a household with annual income of no greater than 300 percent of the area median gross income (within the meaning of that term in section 42) and is eligible to enroll in a public elementary or secondary school.

An organization meets the requirements of a scholarship granting organization (referred to above) only if (a) the organization provides scholarships to two or more students at two or

¹⁴ Treas. Reg. sec. 25.2503-6(c), ex. 2.

¹⁵ Treas. Reg. sec. 25.2503-6(b)(2).

more schools, (b) the organization does not provide scholarships for expenses other than qualified elementary or secondary education expenses, (c) the organization provides scholarships to eligible students with a priority for students awarded a scholarship the previous year and their siblings, (d) the organization does not earmark or set aside contributions for scholarships for any particular student, (e) the organization takes appropriate steps to verify the income and family size of eligible students to whom it awards scholarships, and limits scholarships to individuals in households with annual household income that meets the limits set forth in the definition of an eligible student (the “income verification requirement”), (f) the organization obtains from an independent certified public accountant¹⁶ annual financial and compliance audits and certifies to the Secretary that the audit has been completed, and (g) no officer or board member of the organization has been convicted of a felony.

The term “qualified elementary or secondary education expense” means the following expenses in connection with enrollment or attendance at, or for students enrolled at or attending, an elementary or secondary public, private, or religious school: tuition; curriculum and curricular materials; books or other instructional materials; online educational materials; tuition for certain tutoring or educational classes outside of the home;¹⁷ fees for a nationally standardized norm-referenced achievement test, an Advanced Placement examination, or any examinations related to college or university admission; fees for dual enrollment in an institution of higher education; and educational therapies for students with disabilities provided by a licensed or accredited practitioner or provider. Such expenses include expenses in connection with a homeschool (whether treated as a homeschool or a private school for purposes of applicable State law).

A scholarship granting organization can satisfy the income verification requirement, discussed above, by reviewing all of the following documents (as applicable): (1) Federal and State income tax returns or tax return transcripts with applicable schedules for the taxable year prior to application, (2) income reporting statements for tax purposes or wage and income transcripts from the Internal Revenue Service, (3) notarized income verification letter from employers, (4) unemployment or workers compensation statements, and (5) budget letters regarding public assistance payments and Supplemental Nutrition Assistance Program (“SNAP”) payments including a list of household members.

The credit is a nonrefundable personal tax credit taken against income tax liability. The credit is allowable against both the regular tax and the alternative minimum tax under section 26(a). If the credit allowable for any taxable year exceeds the limitation imposed by section 26(a) for such taxable year reduced by the sum of nonrefundable personal tax credits (other than the individual credit under the proposal and the credits allowable under section 23 and section 25D), the excess is carried to the succeeding taxable year and added to the credit allowable for

¹⁶ For purposes of this requirement, the term “independent certified public accountant” means a certified public accountant who is not a person described in section 465(b)(3)(A) (*i.e.*, having an interest, or being a related person to a person having an interest) with respect to such organization or any employee of such organization.

¹⁷ Such tuition is a qualified expense only if the tutor or instructor is not related to the student and is licensed as a teacher in any State, has taught at an eligible educational institution, or is a subject matter expert in the relevant subject.

such taxable year. However, no credit may be carried forward to any taxable year following the fifth taxable year after the taxable year in which the credit arose. For this purpose, credits are treated as used on a first-in, first-out basis.

The proposal provides rules against self-dealing, such that a scholarship granting organization may not award a scholarship to a disqualified person. For this purpose, a disqualified person is determined pursuant to rules similar to rules in section 4946, and include, for example, substantial contributors, founders, and family members of substantial contributors and founders.

Failure of scholarship granting organizations to make distributions

If the Secretary determines that a scholarship granting organization has not satisfied one or more of the distributional requirements, described below, any contribution made to the organization during the first taxable year beginning after the date of the determination is not treated as a qualified contribution for purposes of the tax credit for individuals created under the proposal.

Under the proposal, the amount of receipts of the scholarship granting organization for the taxable year which are distributed before the distribution deadline with respect to such receipts must be at least equal to the required distribution amount for the taxable year. The “required distribution amount” with respect to a taxable year is equal to 100 percent of the total receipts of the scholarship granting organization for the taxable year, (a) reduced by the sum of the receipts that are retained for reasonable administrative expenses for the taxable year or are carried to the succeeding taxable year, and (b) increased by the amount of carryover from the preceding taxable year. Administrative expenses of a scholarship granting organization are deemed to be reasonable if the expenses do not exceed 10 percent of the organization’s total receipts for the taxable year. At the election of the scholarship granting organization, an amount of up to 15 percent of the total receipts of the organization may be carried to the succeeding taxable year.

Under the proposal, a “distribution” includes amounts which are formally committed but not distributed. A formal commitment may include contributions set aside for eligible students for more than one year. The distribution deadline with respect to receipts for a taxable year is the first day of the third taxable year following the taxable year in which the scholarship granting organization receives the receipts.

Volume cap

The proposal sets an aggregate volume cap on the total amount of credits at \$5 billion for each of calendar years 2025 through 2028, and zero for any calendar years after 2028. However, in the case of the calendar year following a high use calendar year, the volume cap otherwise in effect is increased to 105 percent of the dollar amount in effect for the high use calendar year. The term “high use calendar year” means any calendar year for which 90 percent or more of the volume cap in effect for such calendar year is allocated to taxpayers. The proposal provides that the volume cap in effect for a calendar year must at least equal the volume cap in effect for the

preceding calendar year. Thus, if the volume cap is increased in a year following a high-use calendar year, it is not subsequently reduced.

Generally, for purposes of allocating volume cap for a calendar year, the Secretary is directed to allocate the credit on a first-come, first-served basis, based on the time (during that calendar year) at which the taxpayer made the qualified contribution with respect to which the allocation is made. The Secretary may not allocate volume cap for a calendar year after December 31 of that calendar year. However, 10 percent of the annual volume cap is evenly divided among the States,¹⁸ with such amounts being available to individuals residing in such States. The Secretary is directed to develop a system to track the amount of qualified distributions made during the calendar year for which a credit may be claimed, with such information updated in real time.

Exemption from gross income for scholarships for qualified elementary or secondary education expenses

The proposal provides an exclusion from an individual's gross income for any amounts provided by a scholarship granting organization to the individual's dependent pursuant to a scholarship for qualified elementary or secondary education expenses of an eligible student.

The terms "qualified elementary or secondary education expense," "eligible student," and "scholarship granting organization" have the same meaning given such terms for purposes of the individual credit.

Organizational and parental autonomy

Generally, the proposal provides that (1) a scholarship granting organization is not by virtue of participating under the proposal treated as acting on behalf of a government entity; (2) Federal, State, and local government entities (or officers and employees of such entities) are prohibited from mandating or controlling any aspect of a scholarship granting organization; (3) Federal, State, and local government entities (or officers and employees of such entities) are prohibited from mandating or controlling any aspect of a private or religious elementary or secondary education institution; (4) Federal, State, and local government entities (or officers and employees of such entities) are prohibited from imposing conditions or requirements that would exclude or operate to exclude educational expenses at private or religious elementary and secondary educational institutions from being considered qualified elementary or secondary education expenses, or otherwise disadvantage such institution based on its religious character or affiliation; (5) Federal, State, and local government entities (or officers and employees of such entities) are prohibited from disfavoring or discouraging parents from using scholarships granted by a scholarship granting organization at a private institution, including a faith-based school; and (6) a parent of an eligible student who has received a scholarship from a scholarship granting

¹⁸ For purposes of the volume cap, the term "State" includes the District of Columbia. Therefore, for calendar year 2025, a total of \$500 million (10 percent of \$5 billion) is divided equally among the 50 States and the District of Columbia, with each State receiving approximately \$9.8 million in allocations.

organization has a right to intervene in any court action in which the constitutionality of the proposal has been challenged.

Effective Date

Generally, the proposal is effective on date of enactment. The part of the proposal relating to the tax credit is effective for taxable years ending after December 31, 2024. The part of the proposal relating to the income exclusion for scholarships is effective for amounts received after December 31, 2024, in taxable years ending after December 31, 2024.

B. Estimated Revenue Effects of the Proposal

The proposal is estimated to have the following effect on Federal fiscal year budget receipts:

Fiscal Years [Billions of Dollars]											
<u>2025</u>	<u>2026</u>	<u>2027</u>	<u>2028</u>	<u>2029</u>	<u>2030</u>	<u>2031</u>	<u>2032</u>	<u>2033</u>	<u>2034</u>	<u>2025-29</u>	<u>2025-34</u>
---	-5.5	-4.8	-5.1	-4.2	-0.2	[1]	[1]	[1]	[1]	-19.6	-19.8

NOTE: Details do not add to totals due to rounding.

[1] Loss of less than \$50 million.