NATIONAL EDUCATION ASSOCIATION
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Great Public Schools for Every Student

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Internal Revenue Service
CC:PA:LPD:PR (REG-112176-18)
Room 5203, PO Box 7604
Ben Franklin Station
Washington, DC 20044

On behalf of our three million members, the National Education Association ("NEA") is submitting the following comments on the proposed Treasury Department and IRS amendments (REG-112176-18) to the regulations under IRC Section 170 ("Proposal").[1] NEA, the nation's largest professional employee organization, is committed to advancing the cause of public education. NEA members work at every level of education—from pre-school to university graduate programs, serving 50 million students. NEA has affiliate organizations in every state and in more than 14,000 communities across the United States.

NEA continues to oppose strongly the unfair, and largely political, SALT deduction limitation contained in the Tax Cuts and Jobs Act of 2017 ("TCJA").[2] The deduction for SALT payments has been allowable as long as we have had a federal income tax and should continue to be allowed. This limitation was aimed at taxpayers living in states that have progressive and balanced tax systems and, as a result, many taxpayers in these states will pay more in taxes than they did before the TCJA was passed. This limitation was included in the tax bill to allow for larger corporate and upper-income individual tax cuts to the detriment of middle and lower-income taxpayers. This change in treatment for SALT payments will have a significant impact on the ability of localities and states to raise the revenue necessary for state obligations such as public education. NEA will continue to work with Congress to replace or modify this inequitable outcome.

Proposal

The Proposal was deemed to be necessary by the Treasury Department as a result of the modifications to IRC Section 164 as part of the TCJA that significantly limits the ability of individual taxpayers to deduct payments of state and local taxes.[3] Secretary Mnuchin, and others, raised concerns about states offering tax credits to taxpayers for contributions to state-run

[1] IRS Proposed Regulation [REG-112176-18]: "Contributions in Exchange for State or Local Tax Credits" Notice 2018-172
[2] Tax Cuts and Jobs Act of 2017, PL 115-97
[3] Notice 2018-54, 2018-24 I.R.B. 750, https://www.irs.gov/pub/irs-drop/n-18-54.pdf

charities thereby generating a federal charitable deduction on the contribution. These legislative proposals were being based, in large part, on existing state tax credit regimes that generate federal charitable deductions for taxpayers who also receive state tax credits on the contribution.

NEA generally supports the underlying broad-based approach followed by the Proposal in treating all taxpayers and charitable entities equally and not differentiating between new and existing tax credit regimes. NEA also supports the concept that payments to certain entities can constitute a quid pro quo when the taxpayer receives a state tax credit for the contribution. For many years, the IRS has allowed certain taxpayers to claim a federal charitable tax deduction for contributions to private tax credit scholarship programs ("TCS") even though the taxpayer has received a state tax credit on the same contribution. We are pleased the Proposal will address this loophole. NEA does remain concerned, however, that the Treasury Department has taken the position that the Proposal does not apply to businesses. This distinction creates a significant new tax loophole opportunity for many upper-income taxpayers and should be addressed.

Tax Credit Scholarship Programs

Currently 18 states offer tuition tax credit scholarship programs for individuals and/or businesses with state tax credits ranging from 50% to 100% of the contribution. [4] Taxpayers in such states also have been allowed to claim a charitable deduction on their federal return for the entire amount of their contribution, including the amount upon which they receive the tax credit. Financial planners and advisors have marketed this abuse to encourage clients to get a combined state and federal tax benefit that could be larger than the underlying contribution. As noted in the Proposal, these types of arrangements are inconsistent with sound tax policy. Not only do these programs create the equivalent of a school voucher, but, in some cases, under current rules, they create a federal subsidy in doing so.

These tax credit schemes are part of a larger ongoing effort in many states and by some members of Congress to divert state and federal revenue to private schools. For example, the TCJA created an expansion of IRC Section 529 plan rules in order to allow distributions for K-12 expenses to be qualifying. This new loophole allows upper-income taxpayers in many states to generate a state tax benefit for contributions to 529 plans which can then be simultaneously withdrawn for current K-12 education expenses. This conduit-type of transaction was not the intent of Congress when 529 plans were created to encourage taxpayers to save for their children's college and higher education costs. NEA encourages the IRS and Treasury Department to ensure that sound and fair tax policy is followed and federal revenue is not being diverted away to fund private K-12 schools through loopholes and unintended benefits.

Guidance not Applicable to Businesses

After the Proposal was issued, the IRS released a statement and subsequent FAQ attempting to clarify that businesses will continue to be allowed to deduct the cost of the charitable

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[4] U.S. Gov't Accountability Off., GAO-18-679, *Private School Choice: Requirements for Students and Donors Participating in State Tax Credit Scholarship Programs* (2018) https://www.gao.gov/assets/700/694551.pdf

contribution to TCS programs as ordinary and necessary business deductions under IRC Section 162, and, as such, not affected by the Proposal.[6] This new guidance creates significant new tax abuse concerns, particularly as it relates to the ability of individual taxpayers to use pass-through entities to generate federal tax deductions for contributions that also benefit from state tax credits. In order to be consistent with the tax equity theories espoused in the Proposal, the Treasury Department should expand this Proposal to prevent loopholes to the new SALT deduction limitation.

Conclusion

NEA remains opposed to the unfair and inequitable SALT deduction limitation. We support the approach the Treasury Department and the IRS have taken with the Proposal that treats all charitable deductions for contributions that receive a state tax credit equally and strongly oppose any carve-outs or exceptions made for state tax credit scholarship programs. Finally, we encourage the Treasury Department to expand this Proposal to limit the ability of individual taxpayers to utilize pass-through entities to receive a charitable deduction in cases where it would be denied under this Proposal.

Sincerely,

Marc Egan
Director of Government Relations
National Education Association

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[6] Notice 2018-178