

GENERAL ASSEMBLY OF NORTH CAROLINA

Session 2005

Legislative Fiscal Note

BILL NUMBER: House Bill 770 (First Edition)

SHORT TITLE: Parental Savings Trust Fund Tax Deduction.-AB

SPONSOR(S): Representative Dickson

	FISCAL IMPACT				
	Yes (X)	No ()	No Estimate Available ()		
	(\$ in millions)				
	<u>FY 2005-06</u>	<u>FY 2006-07</u>	<u>FY 2007-08</u>	<u>FY 2008-09</u>	<u>FY 2009-10</u>
REVENUES:					
General Fund	(1.3)	(1.6)	(1.9)	(2.4)	(3.1)
POSITIONS (cumulative):					
PRINCIPAL DEPARTMENT(S) & PROGRAM(S) AFFECTED: North Carolina National College Savings Program, Department of Revenue					
EFFECTIVE DATE: Taxable years beginning on or after January 1, 2005.					

BILL SUMMARY: Under current law, 529 college savings account earnings are state and federal tax-free when used to pay for qualified college expenses. HB 770 allows contributions into the North Carolina National College Savings Program to be tax-deductible up to \$5,000 per beneficiary or \$10,000 per program participant with multiple beneficiaries.

ASSUMPTIONS AND METHODOLOGY: In December 2004, College Foundation Inc. (CFI) stopped accepting financial advisor-sold 529 college savings accounts. CFI had not found the practice of allowing financial advisors to sell the program to investors successful in North Carolina as compared to the national average, and decided it would be best for the program to rely entirely on direct sales. By March 2005, all financial advisors with clients participating in the 529 college savings program had left the program.

CFI believes that making contributions to the National College Savings Program tax-deductible will improve the savings program's national ranking and attract more in-state investors. Every state bordering North Carolina offers a 529 college savings program with some level of tax

deduction proportional to total annual contributions; in Tennessee and West Virginia, the entire yearly contribution is tax-deductible with no fixed upper limit. Additionally, making contributions tax-deductible will require financial advisors who comply with certain professional standards to notify potential investors of the program, potentially expanding the number of program participants.

Because of the loss of program participants due to CFI's change in sales approach, CFI does not anticipate large gains in program enrollment as a result of this legislation; instead, they expect this change will attract new investors that will offset the loss of others, maintaining an annual growth in total contributions between 20-25%.

Based on both historical data and conversations with CFI, the projection below makes the following assumptions:

1. The number of contributions reportable for fiscal year 2004-05 will be lower than in previous years due to the departure of financial advisor-sold program participants. For this reason, the amount of allowable deductions under HB 770 for fiscal year 2005-06 was derived by reducing the 2003-04 amount of allowable deductions by 22%.
2. The average percent growth in allowable deductions was calculated by group. To encourage people to save for college, CFI allows participants to save as little as \$5 a year. Partly for this reason, participants who contribute less than \$5,000 per year regardless of the number of beneficiaries account for the most growth in allowable deductions.

Projected Growth in Allowable Deduction by Category (Variable % changes are derived from actual 2002-2004 data)						
Total contribution per beneficiary	Average % change in allowable deduction	2005-06	2006-07	2007-08	2008-09	2009-10
<i>One beneficiary</i>						
\$5000 or less	31.8%	\$4,718,316	\$6,218,741	\$ 8,196,300	\$10,802,724	\$14,237,990
More than \$5000	2.1%	\$2,406,300	\$2,456,832	\$2,508,426	\$2,561,103	\$2,614,886
<i>Multiple beneficiaries</i>						
\$5000 or less, or less than \$10,000 per participant	37.1%	\$6,565,558	\$9,001,380	\$12,340,893	\$16,919,364	\$23,196,448
More than \$5000, or more than \$10,000 per participant	-0.9%	\$4,659,477	\$4,617,542	\$4,575,984	\$4,534,800	\$4,493,987
Total allowable deduction		\$18,349,652	\$22,294,495	\$27,621,603	\$34,817,990	\$44,543,311
Fiscal impact (at 7%)		\$1,284,476	\$1,560,615	\$ 1,933,512	\$ 2,437,259	\$ 3,118,032

These results approximate the overall 20-25% annual growth anticipated by CFI.

SOURCES OF DATA: College Foundation Inc.

TECHNICAL CONSIDERATIONS: None

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