Franchise Tax Board

ANALYSIS OF AMENDED BILL

Author: Rod Pacheco | Analyst: Darrine Distefano | Bill Number: AB 1224

Related Bills: See Legislative History | Telephone: 845-6458 | Amended Date: 04-02-2001

Attorney: Patrick Kusiak | Sponsor:

SUBJECT: PIT Rates/Reduce All Marginal Tax Rates

SUMMARY

This bill would reduce all existing personal income tax (PIT) rates over a three-year period.

SUMMARY OF AMENDMENTS

The April 2, 2001, amendments eliminated all language regarding discharge of indebtedness and added the new language discussed in this analysis.

PURPOSE OF THE BILL

The purpose of this bill is to alleviate the tax burden for all taxpayers, especially seniors and the middle class.

EFFECTIVE/OPERATIVE DATE

This bill is a tax levy and would be effective upon enactment. It would be operative for taxable years beginning on or after January 1, 2001.

POSITION

Pending.

ANALYSIS

FEDERAL/STATE LAW

Federal law imposes five different income tax rates on individuals ranging from 15% to 39.6%. Existing state law imposes six different PIT tax rates ranging from 1% to 9.3%. Each tax rate applies to a different level of income and is also known as a "tax bracket."

Federal law provides a personal income alternative minimum tax (AMT) rate of 26%. Existing state law also provides a personal income AMT rate of 7%. A taxpayer with substantial income can use preferential tax benefits such as exclusions, deductions, and credits to reduce their income tax liability. AMT was established to ensure that a taxpayer in this situation does not completely escape taxation.

Board Position:			Department Director	Date
____ S	____ NA	____ NP	Alan Hunter for GHG	04/27/01
____ SA	____ O	____ NAR		
____ N	____ OUA	__X__ PENDING		

Existing state law requires the Franchise Tax Board (FTB) to index the tax brackets and the AMT exemption amounts each year to account for inflation.

THIS BILL

This bill would eliminate the lowest PIT rate bracket of 1% for all PIT taxpayers. It also would decrease all remaining PIT tax rate brackets by the year 2003.

The marginal rates proposed by this bill are in the following table:

PITL Marginal Rates			
Current	*2001*	*2002*	*2003*
1%	0%	0%	0%
2%	2%	1%	0%
4%	4%	2%	1%
6%	6%	4%	2%
8%	8%	6%	4%
9.3%	9.3%	8%	6%

This bill would apply to individuals, both residents and nonresidents, sole proprietorships, estates, and trusts.

IMPLEMENTATION CONSIDERATIONS

Implementing the rate reduction would require some changes to existing tax forms and instructions and information systems, which could be accomplished during normal annual update.

LEGISLATIVE HISTORY

AB 955 (Murray, 1993/1994), which failed passage in the Assembly Revenue and Taxation Committee, would have established new amounts for the PIT brackets, the personal exemption credit, and the standard deduction.

AB 643 (Baldwin, 1997/1998), which remained in the Assembly Revenue and Taxation Committee, would have provided a 10% reduction in PIT rates, phased in over two years.

AB 781 (Sweeney, 1997/1998) which was amended and enrolled as the Education Technology Benchmark Implementation Trust Fund, and would have re-established 10% and 11% PIT rates for tax years beginning on or after January 1, 1998, with the additional revenue transferred to the Education Technology Trust Fund.

SB 83 (McPherson, 1997/1998), which remained in the Senate Appropriations Committee, would have eliminated the 1% tax rate bracket for PIT taxpayers and indexed the income threshold amounts for the remaining tax brackets for inflation through the 1996 tax year.

SB 1165 (Hurtt, 1997/1998), which failed passage in the Senate Revenue and Taxation Committee, would have provided a 15% reduction for each of the five rates from 1% to 8% for tax years beginning on or after January 1, 1997; provided a 15% reduction for the 9.3% rate phased in over two years; and created a new marginal rate for taxable income greater than $100,000 which would have been phased out over two years.

SB 1171 (Hurtt, 1997/1998), which was amended to be a sales tax exemption, would have provided a 10% reduction in PIT rates, phased in over two years.

SB 2197 (Rainey, 1997/1998), which failed passage in the Senate Revenue and Taxation Committee, would have increased the threshold amounts of each PIT bracket by 10%.

AB 17 (Hollingsworth, 2001/2002), which is currently in the Assembly Revenue & Taxation Committee, would reduce all existing PIT rates over a five-year period to zero so that income tax for all individuals is eliminated by the year 2005.

OTHER STATES' INFORMATION

The majority of states impose income tax on individuals. Only *Alaska, Florida, Nevada, South Dakota, Texas, Washington,* and *Wyoming* do not have a personal income tax.

FISCAL IMPACT

This bill would not significantly impact the department's costs.

ECONOMIC IMPACT

This bill would result in revenue losses as shown in the following table:

Estimated Revenue Impact*			
Taxable/Income Years Beginning On or After January 1, 2001			
Enactment Assumed After June 30, 2001			
Fiscal Years			
(In Billions)			
	2001-2	2002-3	2003-4
Tax Rate Decreases	-$6.0	-$14.5	-$19.0

*Rounded to nearest half-billion.

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this measure.

<u>Revenue Discussion</u>

The impact of this bill would depend on the amount of tax reductions as a result of a reduction in marginal tax rates, offset by an increase in the alternative minimum tax (AMT). If the author's additional intent were to reduce AMT proportionately, revenue losses would be even higher.

This revenue estimate is based on the department's latest personal income tax model. The proposal would benefit approximately 9.3 million taxpayers for the 2001 tax year. Approximately 985,000 currently taxable returns will become nontaxable as a result of this proposal.

POLICY CONCERNS

This bill does not reference or change AMT. Reducing regular tax rates without a corresponding reduction in AMT rates would result in an increase in the number of taxpayers who would owe AMT.

This bill would provide a tax benefit to low income taxpayers, but would provide a decreasing benefit as taxable income increases due to AMT.

LEGISLATIVE STAFF CONTACT

Darrine Distefano	Brian Putler
Franchise Tax Board	Franchise Tax Board
845-6458	845-6333