

# ANALYSIS OF ORIGINAL BILL

Franchise Tax Board

Author: SR&T Committee Analyst: LuAnna Hass Bill Number: SB 1185

Related Bills: See Legislative History Telephone: 845-7478 Introduced Date: 02-28-2001

Attorney: Patrick Kusiak Sponsor: \_\_\_\_\_

**SUBJECT:** Change B&CT Law to Corp. Tax Law/Electronic Postmarks/Employer Hiring Credit/Vouchering Requirements

## SUMMARY

This Franchise Tax Board sponsored bill would:

- rename the "Bank and Corporation Tax Law" as the "Corporation Tax Law," and
- make California law substantially the same as the federal law that permits electronic postmarks to be proof of the date an e-file return is filed.
- amend the definition of "qualified employee" for specified economic development areas (EDAs) and clarify the vouchering requirements.

The provisions of this bill will be discussed separately.

## BANK AND CORPORATION TAX LAW CHANGES

### PURPOSE OF THE BILL

The purpose of this bill is to make the title of the part of the Revenue and Taxation Code that imposes taxes on corporations consistent with prior legislation that added banks to the definition of corporations.

### EFFECTIVE/OPERATIVE DATE

These provisions would be effective and operative January 1, 2002.

### POSITION

Support.

At its December 18, 2000, meeting, FTB voted 2-0 to sponsor the language introduced in this legislation.

### Summary of Suggested Amendments

The attached amendments would resolve the department's technical concerns discussed below.

Board Position:

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<input type="checkbox"/> N	<input type="checkbox"/> OUA	<input type="checkbox"/> PENDING

Department Director

Date

Gerald H. Goldberg

03/27/01

## **ANALYSIS**

### STATE LAW

Existing state law was revised in 1997 (AB 1040, Revenue and Taxation Committee, Stats. 1997, Ch. 605) in an effort to eliminate unintentional differences that had arisen between the tax treatment of banks and corporations. AB 1040 revised the definition of "corporation" in the Bank and Corporation Tax Law (B&CTL) to include banks, although banks remained subject to tax in a different manner than general corporations. Therefore, the use of the term "bank" in the title of the B&CTL is no longer necessary because banks are included in the definition of a corporation..

### THIS BILL

This bill would make technical, nonsubstantive changes to rename the B&CTL as the "Corporation Tax Law." For consistency, this bill also would rename the Bank and Corporation Tax Fund as the Corporation Tax Fund.

### IMPLEMENTATION CONSIDERATIONS

Implementing these provisions would not significantly impact the department's programs and operations.

### TECHNICAL CONSIDERATIONS

Amendments 6 and 8 are provided to rename Part 11 of Division 2 (and Chapter 2 of the same division) of the Revenue and Taxation Code (R&TC). Amendments 7, 10, 12, and 14 are provided to renumber the sections of the bill.

## **LEGISLATIVE HISTORY**

AB 1040 (Revenue and Taxation Committee, Stats. 1997, Ch. 605), revised the definition of "corporation" in the B&CTL to include banks.

## **PROGRAM BACKGROUND**

California's Bank and Corporation Franchise Tax Act, enacted in 1929, imposes a franchise tax on every corporation and bank doing business within the limits of the state, unless specifically exempt. Among other things, this act implemented the provisions of Section 16 of Article XIII of the California Constitution authorizing a state tax on banks. The term "corporation" as defined within this Act excluded corporations organized as banks. As a result, the state law was entitled the Bank and Corporation Tax Law (B&CTL).

## **OTHER STATES' INFORMATION**

A review of other state tax laws is not relevant to the provisions of this bill relating to the technical changes of the B&CTL.

## **FISCAL IMPACT**

These provisions would not impact the department's costs.

## **ECONOMIC IMPACT**

These provisions would not impact state income tax revenue.

## **ELECTRONIC POSTMARKS**

### **PURPOSE OF THE BILL**

The purpose of this bill is to ensure that the date an electronic return is filed can be properly verified by allowing an electronic postmark to serve as proof a tax return was received timely.

### **EFFECTIVE/OPERATIVE DATE**

These provisions would be effective and operative January 1, 2002, and would apply to all returns filed after that date.

### **POSITION**

Support.

At its December 18, 2000, meeting, FTB voted 2-0 to sponsor the language introduced in this legislation.

### **Summary of Suggested Amendments**

The attached amendments would resolve the department's technical concerns discussed below.

## **ANALYSIS**

### **FEDERAL LAW**

The Internal Revenue Service (IRS) is authorized to issue regulations that extend to electronically filed returns that are similar to those that apply to paper returns sent by registered mail.

The federal regulations regarding electronic postmarks define an electronic return transmitter as an entity that transmits the electronic portion of a return directly to the IRS. An electronic postmark is defined as a record of the date and time that an authorized electronic return transmitter sends the transmission of the taxpayer's electronically filed document.

The federal regulations also provide that the date of an electronic postmark given by an authorized electronic return transmitter will be deemed to be the filing date if the date of the electronic postmark is on or before the filing due date. The Treasury regulations permit the Commissioner to enter into an agreement with an electronic return transmitter or to prescribe in forms, instructions, or other appropriate guidance the procedures under which the electronic return transmitter is authorized to provide taxpayers with an electronic postmark. The electronic postmark acknowledges the date and time that the electronic return transmitter received the electronically filed document.

### STATE LAW

Existing state law provides specific rules for electronic filing. Tax preparers may apply to participate in the California e-file program by submitting an application to FTB, but must already be approved for the federal e-file program by the IRS. A payment voucher for electronically transmitted returns must accompany tax payments made by check. Tax payments also can be made by electronic funds transfer.

When existing state law is in conformity with federal law, the application of federal regulations for state purposes is allowed to the extent those federal regulations do not conflict with regulations issued by FTB.

Existing state law provides penalties for failure to file tax returns by the due date. The due date also applies to electronically filed tax returns; however, there is a five-day "grace period" for error resolution if the return is not transmitted correctly. California allows a six-month automatic paperless extension of time to file returns without the need for specific written requests by taxpayers. If the return is not filed within the extended due date, the automatic extension does not apply and a late filing penalty plus interest is assessed and computed from the original due date of the return. In addition, the extension of time for filing applies only to the due date of the return and does not extend the time for any payment of tax. Tax is due on the original due date of the return, without regard to any filing extension. If the tax is not paid by the due date of the return, an underpayment of tax penalty is imposed.

### THIS BILL

This bill would permit FTB to accept electronic postmarks as proof of the date e-file returns are deemed filed.

### IMPLEMENTATION CONSIDERATIONS

Implementing this bill would assist the department's programs and operations by clarifying and easing administration of the tax law. This bill would provide a clear statutory basis for an electronic postmark to serve as proof that a tax return was received timely and would be consistent with federal practice.

### TECHNICAL CONSIDERATIONS

For consistency within the R&TC, Amendments 4 and 5 are provided to include an additional cross-reference.

## **PROGRAM BACKGROUND**

Treasury Department regulations address the specific rules applicable to timely mailing and electronic postmarks for federal electronically-filed returns. Under these rules, an authorized IRS e-file provider must ensure that it promptly processes returns submitted to it for electronic filing and that returns are transmitted on or before the due date (including extensions).

Existing state law provides that any return that is filed using electronic technology shall be in the form as FTB may prescribe. FTB has generally implemented e-file requirements in FTB Publication 1345, Handbook for Electronic Return Originators. That publication sets forth the roles and responsibilities of transmitters, electronic return originators, tax preparers, and taxpayers when filing electronic income tax returns.

An e-file provider is responsible for the initial receipt of the tax return from the taxpayer or tax practitioner and subsequent transmittal to the IRS and FTB. The electronic postmark that “stamps” each return with the date and time it was first transmitted is used for documentation purposes of timely receipt.

For both state and federal purposes, an electronically filed return is not considered filed until the electronic portion of the tax return has been acknowledged by the IRS or FTB as “accepted for processing.” Currently, neither IRS nor FTB will accept delinquent returns for e-file.

Within 48 hours of receipt, IRS and FTB acknowledge receipt of the electronically filed tax return. The acknowledgment is sent electronically to the e-file provider that then provides it to the taxpayer. The acknowledgment also identifies any error conditions in the tax return.

## **OTHER STATES’ INFORMATION**

Review of Florida, Illinois, Massachusetts, Michigan, Minnesota and New York laws revealed income tax laws pertaining to the acceptance of electronic signatures, although they do not specify whether the transmittal or signature document is equivalent to an electronic postmark. These states were reviewed because of the similarities between California income tax laws and the tax laws of these states.

## **FISCAL IMPACT**

This provision would not impact the department's costs.

## **ECONOMIC IMPACT**

This provision would not impact state income tax revenue.

## **EMPLOYER HIRING CREDIT/VOUCHERING REQUIREMENT**

### **PURPOSE OF THE BILL**

FTB is sponsoring this bill to clarify the vouchering requirements of new employees who qualify for EDA credits and clarify the meaning of “qualified employee.”

## **EFFECTIVE/OPERATIVE DATE**

These provisions would be effective January 1, 2002, and operative for taxable years beginning on or after that date.

## **POSITION**

Support.

At its December 18, 2000, meeting, FTB voted 2-0 to sponsor the language introduced in this legislation.

### **Summary of Suggested Amendments**

The attached amendments would resolve the department's technical concerns discussed below.

## **ANALYSIS**

### STATE LAW

Under existing state law, taxpayers operating in an EDA are allowed a hiring credit for hiring "qualified employees." A "qualified employee" is generally defined by reference as a person who qualifies for at least one of various state or federal public assistance programs.

Existing enterprise zone (EZ), local area military base recovery area (LAMBRA), and targeted tax area (TTA) statutes require taxpayers/employers to obtain vouchers for each new hire to be eligible for the hiring credit. Vouchers are issued by a federal or state agency familiar with the public assistance statutes that comprise the definition of "qualified employee." A voucher is used by FTB at audit to verify that the prospective employee is eligible for or is receiving one of the specified forms of public assistance and thus is a "qualified employee." Existing manufacturing enhancement area (MEA) statutes do not require taxpayers to obtain a voucher to be eligible for the hiring credit.

### THIS BILL

#### Qualified Employee Definition

This bill would clarify the definition of "qualified employee" by adding a specific reference to the definitions of the federal Job Training Partnership Act (JTPA) as they existed on and before June 30, 2000.

#### Vouchering Requirement

This bill would clarify that there must be a voucher for each new employee by adding the vouchering requirement to the definition of "qualified employee."

This bill would allow a taxpayer the opportunity to substantiate independently that an employee is a "qualified employee" where no vouchering process has been established.

## IMPLEMENTATION CONSIDERATIONS

These provisions would improve the department's ability to administer the laws relating to the EDA hiring credits by specifying the vouchering requirement and by providing the department necessary flexibility in circumstances where no voucher can be obtained due to no fault of the taxpayer. These changes could be implemented during the department's normal annual update.

## TECHNICAL CONSIDERATIONS

This bill requires a voucher for each new employee. Amendments 1-3, 9, 11, and 13 would provide a specific cross-reference within the definition of "qualified employee" clarifying that the employee must be certified.

## **LEGISLATIVE HISTORY**

AB 2895 (Assembly Revenue and Taxation Committee, Stats. 2000, Ch. 864) amended the LAMBRA and MEA hiring credit statutes to include a vouchering requirement. However, the vouchering requirement for the MEA added by AB 2895 was chaptered out of law by SB 1445 (Kelley, Stats. 2000, Ch. 865).

## **PROGRAM BACKGROUND**

### Qualified Employee Definition

The hiring credits allowed to taxpayers in EDAs may be claimed by an employer (the taxpayer) for a percentage of wages paid to a new employee. The taxpayer may claim a hiring credit only for a "qualified employee." A "qualified employee" is defined as a person who falls within an extensive list of economically disadvantaged individuals. This list includes individuals who are recipients of assistance under several specifically named federal and state public assistance programs. One of those programs is the federal JTPA.

In 1997, the Trade and Commerce Agency (TCA) became concerned about the pending expiration of JTPA. TCA was concerned that the statutory basis for determining whether a new employee was a "qualified employee" would cease to exist when JTPA expired. TCA requested that the R&TC definition of "qualified employee" be amended by adding paraphrased versions of the underlying definitions of persons eligible for JTPA under federal law. Accordingly, legislation was enacted that defined "qualified employee" with the extensive list of economically disadvantaged individuals.

### Vouchering Requirement

The hiring credit statutes provide that the taxpayer "shall" obtain and retain a certification (voucher) document that certifies that a new employee met the eligibility requirement of a "qualified employee." The intent of the vouchering requirement was to make receipt of a voucher a prerequisite to claiming the credit. The voucher is used to track and control the value of the EDA programs by TCA and to promote consistent application of the elements that must be satisfied to receive the hiring credit.

## **OTHER STATES' INFORMATION**

A review of other state tax laws is not relevant to the provisions of this bill relating to the definition of "qualified employee" as used in specifically listed EDAs since these provisions make only minor technical changes to current state law.

## **FISCAL IMPACT**

These provisions would not impact the department's costs.

## **ECONOMIC IMPACT**

These provisions clarify current law hiring credit conditions. No further revenue impact would result.

## **LEGISLATIVE STAFF CONTACT**

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FRANCHISE TAX BOARD'S  
PROPOSED AMENDMENTS TO SB 1185  
As Introduced February 28, 2001

AMENDMENT 1

On page 3, modify line 39 as follows:

(iv) Is certified as provided in paragraph (1) of subdivision (d) as any of the following:

AMENDMENT 2

On page 13, modify line 9 as follows:

(C) Who is certified as provided in paragraph (1) of subdivision (c) as any of the following immediately preceding the

AMENDMENT 3

On page 22, modify line 25 as follows:

(iv) Is certified as provided in paragraph (1) of subdivision (c) as any of the following:

AMENDMENT 4

On page 34, modify line 16 as follows:

Section 17001), Part 10.2 (commencing with Section 18401), Part 11 (commencing with Section 23001), or this

AMENDMENT 5

On page 34, modify line 19 as follows:

(commencing with Section 17001), Part 10.2 (commencing with Section 18401), Part 11 (commencing with

AMENDMENT 6

On page 35, line 6, after "SEC. 12.," insert:

Part 11 of Division 2 of the Revenue and Taxation Code is amended to be entitled:  
"Corporation Tax Law"

Sec. 13.

AMENDMENT 7

On page 35, line 10, ~~strikeout "SEC. 13.,"~~ and insert:

SEC. 14.

AMENDMENT 8

On page 35, line 21, ~~strikeout "SEC. 14.,"~~ and insert:

SEC. 15. Chapter 2 of Part 11 of Division 2 of the Revenue and Taxation Code to be entitled:

"The Corporation Franchise Tax"

Sec. 16.

AMENDMENT 9

On page 37, modify line 1 as follows:

(iv) Is certified as provided in paragraph (1) of subdivision (c) as any of the following:

AMENDMENT 10

On page 44, line 29, ~~strikeout "SEC. 15.,"~~ and insert:

SEC. 17.

AMENDMENT 11

On page 46, modify line 6 as follows:

(iv) Is certified as provided in paragraph (1) of subdivision (d) as any of the following:

AMENDMENT 12

On page 54, line 6, strikeout "SEC. 16.," and insert:

SEC. 18.

AMENDMENT 13

On page 55, modify line 28 as follows:

(C) Who is certified as provided in paragraph (1) of subdivision (c) as any of the following immediately preceding the

AMENDMENT 14

On page 63, line 30, strikeout "SEC. 17.," and insert:

SEC. 19.