Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author:	Aghazarian	Analyst:	Kristina E. North	Bill Number:	AB 339
Related Bills:	See Legislative History	Telephone:	845-6978	Introduced Date:	February 11, 2003
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Farmworker Housing Credits/Decrease Compliance Period To 10 Years

SUMMARY

This bill would:

- decrease the period for which the farmworker housing credit is allowable; and
- allow any taxpayer to be eligible for the credit regardless of actual ownership.

PURPOSE OF THE BILL

According to the author's office, the purpose of this bill is to encourage more participation in building farmworker housing.

EFFECTIVE/OPERATIVE DATE

This bill would be effective January 1, 2004, and would apply to farmworker housing credits on or after January 1, 2004.

POSITION

Pending.

ANALYSIS

STATE LAW

Current federal law requires that, for low-income housing credits, a partner's distributive share of income, gain, loss, deduction, or credit be determined pursuant to the partnership agreement. If 1) the partnership agreement does not provide the partner's distributive share of the credit, or 2) the allocation to a partner does not have substantial economic effect, the partner's distributive share is determined pursuant to the partner's interest in the partnership.

Current state law for low-income housing credits conforms to federal law with some modifications. State law does not allow consolidated returns. For the low-income housing credit, however, state law provides similar treatment by allowing a corporation to assign any portion of the low-income housing credit to one or more affiliated corporations, provided the affiliation is 100% ownership.

Board Position:			Department Director	Date
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Current state law allows a taxpayer/owner of farmworker housing a credit for 50% of the qualified amount of costs for the construction or rehabilitation of qualified farmworker housing. The credit is based on the low-income housing credit. The housing must be in California and satisfy the requirements of the Farmworker Housing Assistance Program (Program). Commercial lenders are allowed a credit equal to 50% of the foregone interest income on loans used to finance qualified expenditures for qualified farmworker housing. The California Tax Credit Allocation Committee (Committee) oversees the Program and allocates the credits.

The owner must maintain the housing produced under the Program as farmworker housing for a 30-year "compliance period." The compliance period begins with the first taxable year in which the credit is allowable. If a taxpayer does not meet the requirements of the Program, the Committee is required to promptly notify the Franchise Tax Board (FTB) of any disqualifying event. FTB must then add a prorated "recapture" amount of the previously allowed credit to the taxpayer's tax liability in the taxable year in which the disqualifying event occurs. The recapture amount is determined by multiplying the total amount of the previously allowed credit by a fraction. The numerator would be the number of years remaining in the taxpayer's compliance period, and the denominator would be 30 (the total compliance period).

THIS BILL

Under both the California Health and Safety Code and California tax law, this bill would reduce the compliance period for the farmworker housing credit from 30 years to 10 years.

This bill would expand the California Health and Safety Code to allow the Committee to issue a credit to any person or entity, regardless of whether they own or have an economic interest in the farmworker housing for which the credit is claimed.

IMPLEMENTATION CONSIDERATIONS

This bill would allow the Committee to consider any person or entity eligible for the farmworker housing credit, regardless of actual farmworker housing ownership. Thus, the Committee could allocate the credit to a person with no economic interest in the property, making recapture of the credit more difficult. Recapture provisions could be further complicated in that the recipient of the tax credit may have no direct or indirect control over what the owner or operator do in terms of future compliance with the credit requirements.

The author has indicated the bill is not intended to alter the compliance period for previously allocated credits. To eliminate the possibility of disputes at audit in this regard, the author may wish to consider amending the bill to clarify that the reduction in the compliance period from 30 years to 10 years would not apply to any credit allocated prior to the date the bill was introduced, the effective date of the bill, or some other specified date.

If the bill is not amended to specify that the reduction in the compliance period is not intended to be retroactive, the taxpayer with the existing credit could attempt to claim the reduction applies to his or her credit. However, since the farmworker housing credit is based on a contractual agreement between the Committee and the credit recipient, any credits issued prior to the effective date of this bill may not be entitled to the reduction in the compliance period without a contractual revision specifying that the shorter compliance period would apply.

<u>TECHNICAL CONSIDERATION</u>

AB 1843 (Ackerman, Stats. 2000, Ch. 862) replaced references to “income year” with “taxable year” in the Revenue and Taxation Code. For consistency, the author may wish to amend Health and Safety Code Section 50199.50(b) to remove the obsolete “income year” reference.

LEGISLATIVE HISTORY

AB 1811 (Reyes; Ch. 311, Stats 2000) made various changes to the Farmworker Housing Assistance Program.

SB 1903 (Lowenthal, vetoed 2000) would have allowed the state low-income housing credit to be distributed among partners pursuant to a partnership agreement, even if the allocation of that credit did not have substantial economic effect. Governor Davis vetoed this bill on September 30, 2000.

SB 302 (Costa; Ch. 311, Stats. 1998) redefined the basis for the farmworker housing credit as "eligible costs" and made other minor changes.

SB 38 (Lockyer; Ch. 954, Stats. 1996) created the Farmworker Housing Assistance Program and allowed the assignment of the related farmworker housing credit.

PROGRAM BACKGROUND

The Committee may issue up to $500,000 in farmworker housing credits per year. According to Committee staff, only one credit has been issued since the program was established in 1996, and no other allocation of credits have been proposed or are pending.

OTHER STATES’ INFORMATION

Illinois, Massachusetts, Michigan, Minnesota, and *New York* laws do not provide a credit comparable to the credit allowed by this bill. The laws of these states were reviewed because their tax laws are similar to California’s income tax laws. *Florida* has only a corporation income tax therefore this personal income tax credit is not applicable.

FISCAL IMPACT

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

ECONOMIC IMPACT

<u>Revenue Estimate</u>

Tax return data indicates that only one farmworker housing tax credit has been claimed since the program’s inception and it did not exceed $10,000 per year. Assuming that this bill would have some positive incentive effect pertaining to farmworker housing, the additional revenue loss would most likely be negligible.

POLICY CONCERN

This bill would disconnect ownership of the property from eligibility for the credit, thus severing the credit from a taxpayer's economic interest in the profits and losses of the project. Since the Committee could issue this credit to any partnership, corporation, or business entity, this action could lead to allocations for tax shelter purposes. For example, investors would be able to "buy" rights to farmworker housing credits through the purchase of a partnership share. When all of the credits (which could exceed the cost of their investments) have been utilized, the investor could walk away from the partnership with a negative basis against other income. Thus, the investor would benefit twice from the arrangement: first by use of the credit and second by the negative basis. Governor Davis vetoed a similar proposed change to the low-income housing credit on September 30, 2000, citing his concern with "abuses that may arise" from the severance of economic interest in the project and the potential for allocations being obtained for tax shelter purposes.

LEGISLATIVE STAFF CONTACT

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