BILL ANALYSIS

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Department, Board, Or Commission	Author	Bill Number
Franchise Tax Board	**Florez**	**SB 114**

SUBJECT

Disaster Loss Deduction and Excess Loss Carryover for Specified Counties for the Freezing Conditions that Occurred on January 11, 2007

SUMMARY

This bill would allow taxpayers special tax treatment, called disaster loss treatment, for losses sustained as a result of the January, 2007, freezing conditions.

PURPOSE OF BILL

According to the author's office, the purpose of the bill is to provide immediate tax relief to individuals and businesses affected by the freezing conditions of January 11, 2007.

EFFECTIVE/OPERATIVE DATE

As an urgency measure, this bill would be effective and operative immediately upon enactment.

ANALYSIS

FEDERAL/STATE LAW

Under federal and state law, a disaster loss occurs when business and personal property is destroyed as a result of a fire, storm, flood, or other natural event in an area proclaimed to be a disaster by the President of the United States.

Under federal and state tax law, individual and business taxpayers may elect to claim the loss either in the year the loss occurs or in the year preceding the loss. This election allows the taxpayer to file an amended return immediately for the prior year.

Under federal and state law, individual taxpayers with non-business disaster losses that are not reimbursed by insurance or otherwise, are deductible to the extent each loss exceeds $100 or 10% of adjusted gross income.

State tax law identifies specific events as disasters that are then allowed additional special carry forward treatment. That is, 100% of the excess disaster loss may be carried over for up to five taxable years, and if any excess loss remains after the five-year period, the remaining excess loss may be carried over at a specified percentage for up to ten additional years. In addition, for disasters that were not the subject of a Presidential disaster declaration, state law authorizes the deduction of a disaster loss on the return for the prior year if the disaster was the subject of a Governor's proclamation.

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THIS BILL

This bill would add the freezing conditions that occurred in this state commencing January 11, 2007, to the current list of specified disasters under the Personal Income Tax Law and the Corporation Tax Law. The counties included in the bill's provision are El Dorado, Fresno, Imperial, Kern, Kings, Madera, Merced, Monterey, Riverside, San Bernardino, San Diego, San Luis Obispo, Santa Barbara, Santa Clara, Stanislaus, Tulare, Ventura, and Yuba Counties.

Specifically, this bill would allow a taxpayer to elect to claim the loss either in the year the loss occurred or in the year preceding the loss. If a taxpayer elects to take the loss in the preceding year, this bill would allow the taxpayer to file an amended return immediately for the prior year.

This bill also contains double jointing language that would incorporate provisions from SB 38 (Battin) and AB 62 (Nava) that would allow taxpayers affected by the fires that occurred in Riverside and Ventura Counties in 2006 and El Dorado, Santa Barbara, and Ventura Counties in 2007, disaster loss treatment for their losses.

LEGISLATIVE HISTORY

AB 62 (Nava) and SB 38 (Battin) of 2007/2008 would allow taxpayers disaster loss treatment for losses sustained in Riverside and Ventura counties as a result of the wildfires that occurred in September, 2006, and October, 2006. These bills have been enrolled.

AB 164 (Stats. 2005, Ch. 623), AB 1798 (Stats. 2006, Ch. 896), AB 2735 (Stats. 2006, Ch. 897), , and SB 457 (Kehoe, Stats. 2005, Ch. 622) allowed taxpayers disaster loss treatment for losses sustained as a result of the Santa Barbara, Ventura, Humboldt, Lake Mendocino, Napa, Sonoma, and Trinity County Severe Rainstorms, Related Flooding, Slides, and other events.

AB 18 (La Malfa, Stats. 2005, Ch. 624) allowed taxpayers disaster loss treatment for losses sustained as a result of the Shasta County wildfires.

AB 1510 (Kehoe, Stats. 2004, Ch. 772) allowed taxpayers disaster loss treatment for losses sustained as a result of the following disasters: the Middle River levee break in San Joaquin County, the Southern California wildfires, floods, mudflows, and debris flows directly related to the Southern California wildfires and the San Simeon earthquake.

PROGRAM BACKGROUND

On February 15, 2007, Governor Schwarzenegger proclaimed 18 counties to be in a state of emergency due to the freeze of January, 2007. The 18 counties designated in the proclamation include El Dorado, Fresno, Imperial, Kern, Kings, Madera, Merced, Monterey, Riverside, San Bernardino, San Diego, San Luis Obispo, Santa Barbara, Santa Clara, Stanislaus, Tulare, Ventura, and Yuba.

On March 13, 2007, President George W. Bush declared 12 counties in California as a federal disaster, as a result of the January, 2007, freeze, 11 of which were also declared by the Governor. The 12 counties designated as federal disaster areas include Fresno, Imperial, Kern, Los Angeles, Monterey, Riverside, San Bernardino, San Diego, San Luis Obispo, Santa Barbara, Tulare, and Ventura Counties. Los Angeles County was excluded from the Governor's proclamation. The President's declaration excludes El Dorado, Kings, Madera, Santa Clara, Stanislaus, and Yuba Counties. As a result, these six counties will need state legislation to be enacted in order to receive disaster loss treatment.

OTHER STATES' INFORMATION

Michigan, Minnesota, Massachusetts, and *New York* conform to the federal provisions that allow taxpayers to claim a disaster loss deduction on their state tax returns either in the preceding year or in the year of the loss. It appears that legislation, executive order, or proclamation by the President or the Governor is required to identify the area impacted by a disaster that is eligible for federal or state assistance.

Florida does not have a personal income tax; however, monetary relief is provided to citizens and corporations through the Emergency Management, Preparedness, and Assistance Trust Fund. *Florida* also requires legislation, executive order, or proclamation to identify the area impacted by a disaster.

FISCAL IMPACT

This bill would not impact the department's costs.

ECONOMIC IMPACT

Based on the data and assumptions discussed below, the revenue impact from this bill would be as follows:

Revenue Analysis for SB 114 Effective Immediately and Operative January 1, 2006 Enactment assumed before June 30, 2007				
Fiscal Year	2006-07	2007-08	2008-09	Cumulative Impact
Freeze Disaster Relief	Loss < -$250,000	Gain < $150,000	Gain < $150,000	Loss < -$150,000

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

Revenue Discussion

According to data from the Department of Food and Agriculture, it is estimated that $1.5 billion in total crop damages occurred in California as a result of the January, 2007, freeze. Based on media reports, it is estimated that approximately 85% of the freeze-impacted crops are covered by insurance and would therefore not be affected by this bill (15% uninsured x $1.5B statewide = $225 million uninsured). Under existing law, financial losses from the reduction in value of unharvested crops are not deductible under the casualty loss rules because crops have zero income tax basis. Hence, the relevant impact of this bill will primarily depend on the extent of non-crop losses to farming operations damaged by the freeze. For example, the reduction of the book value of a depreciable asset (e.g. tree, irrigation pipe, etc.) by the fair market value (e.g. appraisal value) would result in a disaster loss.

This estimate assumes that tax-deductible losses will be equivalent to 5% of the $225 million of uninsured losses (roughly $11 million). If 20% of such losses were applied to the preceding year, an estimated $180,000 of refunds would be accelerated ($11 million x 20% x 8% tax rate). The insignificant revenue gains in the later years are a matter of a timing event. Taxpayers that chose to file an amended return to report the casualty loss immediately will have a higher tax liability in the latter income years.

VOTES

Assembly Floor – Ayes: 36, Noes: 0
Senate Floor – Ayes: 78 , Noes: 0
Concurrence – Ayes: 39, Noes: 0

LEGISLATIVE STAFF CONTACT

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