Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author:	Cogdill	Analyst:	Nicole Kwon	Bill Number:	SB 417
Related Bills:	See Legislative History	Telephone:	845-7800	Introduced Date:	February 21, 2007
		Attorney:	Daniel Biedler	Sponsor:	

SUBJECT: Sales Or Use Tax Paid For Qualified Property Used In Enterprise Zones Credit/Allow Remaining Costs Above $20 Million Limit To Be Taken In Account In Following & Subsequent Taxable Years

SUMMARY

This bill would modify the Enterprise Zone (EZ) sales or use tax credit.

PURPOSE OF THE BILL

According to the author's office, the purpose of this bill is to provide a greater incentive for large investments in economically distressed parts of the state.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately upon enactment, and operative for taxable years beginning on or after January 1, 2007.

POSITION

Pending.

Summary of Suggested Amendments

Technical amendments are necessary and are provided. Department personnel are available to work with the author to resolve any other issues that arise as the bill moves through the legislative process.

ANALYSIS

FEDERAL/STATE LAW

Existing federal law provides for the existence of empowerment zones and enterprise communities to provide economic revitalization of distressed urban and rural areas.

Board Position:			Department Director	Date
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Under the Government Code, existing state law allows the governing body of a city or county to apply for designation as an EZ. Using specified criteria, Department of Housing and Community Development designates EZs from the applications received from the governing bodies.

Certain taxpayers conducting business activities in an EZ are permitted special tax incentives under the Revenue and Taxation Code. These incentives include a sales or use tax credit for the purchase of qualified property, as defined, that is used by a qualified taxpayer, as defined, in an EZ. Currently, the credit is for the sales or use tax paid with respect to the total cost of qualified property purchased and placed in service in any taxable year. However, the total costs of qualified property that may be taken into account cannot exceed $1 million under the Personal Income Tax Law (PITL) or $20 million under the Corporation Tax Law (CTL) in any particular taxable year.

A qualified taxpayer under the CTL is defined as a corporation engaged in a trade or business within an EZ. Business includes manufacturing, textiles, freight, transportation, warehousing and storage, and durable and non-durable wholesale goods, as specified by the Standard Industrial Classification (SIC) Manual published by the U.S. Office of Management and Budget, 1987 edition.

THIS BILL

This bill would allow qualified costs in excess of the CTL $20 million annual limitation to be taken into account in the following and succeeding taxable years, not to exceed $20 million per year, in calculating the sales or use tax credit in those succeeding years.

IMPLEMENTATION CONSIDERATIONS

This bill is silent about what would happen to the provisions of this bill when an EZ designation expires, namely will the taxpayer be able to carryover the excess credit amount even though the EZ no longer exists. Amendment 1 is provided to address the carryover provision.

This bill would allow taxpayers to carry forward to future years otherwise qualified costs of qualified property in excess of $20 million, which raises a number of complex tax accounting issues for both the taxpayers and the department regarding tracking the depreciable basis of qualified property. The language is not clear if the author’s intention is to allow taxpayers to receive this credit in later years related to costs paid or incurred in an earlier year in excess of $20 million. If this is the author’s intention, the language should be amended to allow for the computation of credits in the year placed in service, with a per-year limitation on the amount that can actually be used against the tax. Then the amount over $20 million could be carryover credits, with limitation, to later years. Such an approach would continue to limit the amount of current credit that taxpayers could apply against the tax in each year to $20 million of costs, while still allowing the taxpayer to utilize credits in excess of that limitation in later years. The language in Revenue and Taxation Code section 17052.17 uses an approach similar to that suggested above. Department staff is available to work with the author’s office to resolve the implementation concern.

LEGISLATIVE HISTORY

SB 1001 (Ashburn, 2005/2006) would have increased the qualified property limitation for the Targeted Tax Area sales and use tax credit from $1 million to $10 million under the PITL and from $20 million to $50 million under the CTL. SB 1001 failed to pass out of Senate Revenue & Taxation Committee.

FISCAL IMPACT

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

ECONOMIC IMPACT

Revenue Estimate

Based on data and assumptions discussed below, this provision would result in the following revenue losses.

Estimated Revenue Impact of SB 417 Effective for Tax Years BOA 1/1/2007 Assumed Enactment Date After 6/30/2007 ($ in Millions)		
2007/08	2008/09	2009/10
<-$.5	-$1	-$1

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

Revenue Discussion

The revenue impact of this bill is the amount of additional EZ sales or use tax credit that would be utilized to reduce corporate tax liabilities as a result of the proposed modification. The proposed modification would allow a carryover of the cost of qualified property in excess of the $20 million per tax year limit on qualified property costs. The costs carried over could be included in subsequent tax year's $20 million limitation on qualified property costs.

Review of actual corporate income/franchise tax data for tax years 2001 through 2004 indicates this provision would affect less than 10 taxpayers per year, and the annual revenue loss would be approximately $1 million per year. Estimates in the table above have been converted to fiscal years.

POLICY CONSIDERATION

This bill would provide a carryover provision only for corporations that would not be provided to personal income taxpayers. Thus, this bill would provide differing treatment based solely on classification.

LEGISLATIVE STAFF CONTACT

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FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO SB 417
As Introduced February 21, 2007

AMENDMENT 1

On page 4, after line 15, insert:

(5) In the event that a credit carryover is allowable under subdivision (d) for any taxable year after the enterprise zone designation has expired, has been revoked, is no longer binding, or has become inoperative, the enterprise zone shall be deemed to remain in existence for purposes of computing the limitation specified in this subdivision.