Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author:	Migden	Analyst:	John Pavalasky	Bill Number:	SB 758
Related Bills:	None	Telephone:	845-4335	Introduced Date:	February 23, 2007
		Attorney:	Douglas Powers	Sponsor:	

SUBJECT: Exclusion/Gain From Sale Of Stock In Agricultural Refiners & Processors To Farm Cooperatives

SUMMARY

This bill would permit an exclusion from income for gains from the sale of certain food refiners and processors to eligible farmers' cooperatives in conformity with federal law.

PURPOSE OF THE BILL

According to the author's office, the purpose of the bill is to provide tax fairness for farmers by conforming California's tax law with federal law allowing agricultural processors to receive tax-deferred status for sales of processing facilities to an eligible farmers' cooperative.

EFFECTIVE/OPERATIVE DATE

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

POSITION

Pending.

SUMMARY OF SUGGESTED AMENDMENTS

Technical amendments are necessary and have been provided to the author.

ANALYSIS

FEDERAL/STATE LAW

Current Federal Law

Starting in 1998, the Taxpayer Relief Act of 1997 amended the Internal Revenue Code (IRC) to permit owners of certain "qualified refiners and processors" to exclude from current federal taxation the gain from the sale of their stock to "eligible farmers' cooperatives."

Board Position:			Department Director	Date
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The gain from the sale generally will not be recognized to the extent that the sales proceeds are timely invested in qualified replacement property. This property generally includes the stock or securities of an unrelated domestic operating corporation that did not have excessive passive investment income. The basis of the qualified replacement property is reduced by any unrecognized gain. Thus, the recognition of such gain is deferred until the qualified replacement property is sold.

A “qualified refiner or processor” is a domestic corporation (including an S corporation):

- Where substantially all of the activities of which consist of the active conduct of the trade or business of refining or processing agricultural or horticultural products; and

- That purchases more than one-half of the products to be refined or processed, for at least one year prior to the sale, from farmers who make up the cooperative (or the cooperative itself) that is purchasing the stock.

An “eligible farmers’ cooperative” is an organization that is treated as a cooperative for federal income tax purposes and is engaged in the marketing of agricultural or horticultural products.

The provision applies only if, immediately after the sale, the “eligible farmers’ cooperative” owns 100% of the “qualified refiner or processor.” The provision applies even if the stock of the “qualified refiner or processor” is publicly traded. In addition, the provision applies to gain on the sale of stock by a corporation.

Current California Law

California does not conform to this federal provision. Thus, the gain on the sale of stock by owners of food refiners is included in income and taxed by California in the year of sale. Additionally, the federal basis reduction of replacement property does not apply under California law, which has the effect of California taxing a smaller amount of gain on the subsequent sale of that federal replacement property.

THIS BILL

Starting in 2007, this bill would, in conformity with federal income tax law, permit owners of certain qualified refiners and processors to exclude from current California taxation the gain from the sale of their stock to eligible farmers’ cooperatives.

TECHNICAL CONSIDERATIONS

Technical amendments are necessary and have been provided to the author.

OTHER STATES' INFORMATION

The states surveyed include *Florida, Illinois, Massachusetts, Michigan, Minnesota,* and *New York.* These states were selected due to their similarities to California's economy, business entity types, and tax laws. Computation of state taxable income starts with federal adjusted gross income (AGI) for individuals or federal taxable income (TI) for corporations in each of these states. *Florida, Illinois, Massachusetts, Michigan, Minnesota,* and *New York* do not require an adjustment to add back to state income the gain on the sale of stock by owners of food refiners and, thus, have conformed to that federal exclusion.

FISCAL IMPACT

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

ECONOMIC IMPACT

Revenue Estimate

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

Estimated Revenue Impact of SB 758 As Introduced 2/23/07 ($ in Millions)		
2007-08	2008-09	2009-10
<$0.25	<$0.25	<$0.25

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 the bill is determined by the amount of otherwise taxable gains that are deferred under the bill and tax rates of taxpayers selling qualified securities. Estimates are based on a proration of low-level federal projections developed for the Taxpayer Relief Act of 1997.

LEGISLATIVE STAFF CONTACT

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