Franchise Tax Board

ANALYSIS OF AMENDED BILL

Author:	Furutani	Analyst:	Matthew Cooling	Bill Number:	AB 1836
Related Bills:	See Legislative History	Telephone:	845-5983	Amended Date:	April 5, 2010
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: PIT Rates/Increase Maximum Rates To 10 Percent & 11 Percent & AMT To 8.5 Percent Beginning On Or After January 1, 2011, & Before January 1, 2016

SUMMARY

This bill would establish temporary income tax rates of 10 percent and 11 percent and would increase the Alternative Minimum Tax (AMT) rate to 8.5 percent, as specified.

SUMMARY OF AMENDMENTS

The April 5, 2010, amendments added language that would revise the Personal Income Tax Laws (PITL) to establish tax brackets for taxpayers with taxable income in excess of $250,000. The amendments removed provisions that would have made non-substantive changes related to the sales tax exclusion for rental properties.

This is the department's first analysis of the bill.

PURPOSE OF THE BILL

According to the language of this bill, the purpose is to provide a steady revenue stream that gives funding for education and vital health and safety services.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2011, and before January 1, 2016.

POSITION

Pending.

ANALYSIS

FEDERAL/STATE LAW

Federal tax law imposes six different income tax rates on individuals, estates, and trusts ranging from 10 percent to 35 percent.

Board Position:			Department Director	Date
_______ S	_______ NA	_______ NP		
_______ SA	_______ O	_______ NAR	Selvi Stanislaus	04/26/10
_______ N	_______ OUA	___X___ PENDING		

For taxable years beginning on or after January 1, 2009, and before January 1, 2011, state tax law imposes six different rates under the PITL ranging from 1.25 percent to 9.55 percent. Each tax rate applies to different ranges of income, known as "tax brackets." Current state tax law requires the Franchise Tax Board to recalculate the tax brackets each year based on the change in the California Consumer Price Index (CCPI).

Current state law imposes an additional 1 percent Mental Health Tax (MHT), not subject to reduction by credits, on the portion of a Personal Income Tax (PIT) taxpayer's taxable income that exceeds $1 million. The taxable income threshold of $1 million is not indexed based on changes in the CCPI. The MHT is subject to estimated tax payment requirements, interest, penalty, and other tax administration rules applicable to other taxes imposed under the PITL.

Federal law provides an AMT rate of 26 percent on alternative minimum taxable income up to $175,000 and 28 percent on alternative minimum taxable income exceeding that amount for PIT taxpayers. Current state PIT law provides an AMT rate of 7.25 percent for taxable years beginning on or after January 1, 2009, and before January 1, 2011. A taxpayer with substantial income can use preferential tax benefits, such as exclusions, deductions, and credits, to reduce their income tax liability. AMT was established to ensure that a taxpayer who can use preferential tax benefits does not completely escape taxation.

<u>THIS BILL</u>

This bill would establish a PIT rate of 10 percent for the following:

- Single filers (including married/RDPs filing separate, trusts, and estates) whose taxable income is over $250,000 and equal to or less than $400,000,
- Joint filers whose taxable income is over $500,000 and equal to or less than $800,000, and
- Head of household filers whose taxable income is over $400,000 and equal to or less than $600,000.

This bill would establish a PIT rate of 11 percent for the following:

- Single filers (including married/RDPs filing separate, trusts, and estates) whose taxable income is over $400,000,
- Joint filers whose taxable income is over $800,000, and
- Head of household filers whose taxable income is over $600,000.

For taxable years beginning on or after January 1, 2011, and before January 1, 2016, this bill would increase the AMT rate from 7 percent to 8.5 percent.

This bill specifies that the amount of tax imposed by the increased tax rates would be reduced on a dollar-for-dollar basis by an amount equal to the MHT imposed. For example, a taxpayer whose taxable income is $1.5 million would be subject to a $5,000 MHT, to be deposited into the Mental Health Services fund. Under this bill, the $5,000 MHT imposed would be subtracted from the amount of the taxpayer's total tax liability under the increased rates imposed under the bill.

<u>IMPLEMENTATION CONSIDERATIONS</u>

Implementing this bill would require some changes to existing tax forms and instructions and information systems, which could be accomplished during the normal annual update.

<u>TECHNICAL CONSIDERATION</u>

It is recommended that the author delete no longer operative deadwood language related to a Department of Finance determination resulting in alternative tax rates.

LEGISLATIVE HISTORY

SB 96 (Ducheny, 2009/2010) would have added PIT rates of 9 percent, 9.5 percent, 10 percent, 10.5 percent, and 11 percent and increased the AMT rate for PIT taxpayers to 8.5 percent. SB 96 failed to pass out of the house of origin by the constitutional deadline.

AB 2897 (Hancock, 2007/2008) would have established PIT rates of 10 percent and 11 percent and increased the AMT rate for PIT taxpayers to 8.5 percent. AB 2897 failed passage out of the Assembly Revenue and Taxation Committee.

AB 6 (Chan, 2005/2006) would have established PIT rates of 10 percent and 11 percent and increased the AMT rate for PIT taxpayers to 8.5 percent. This bill also would have reduced the amount of tax paid under the increased tax rates by the amount of tax imposed under Proposition 63, the MHT. AB 6 failed to pass out of the house of origin by the constitutional deadline.

Proposition 63 (Steinberg), approved by voters in the November, 2004, General Election, imposes a 1 percent tax on taxable incomes in excess of $1 million to provide a dedicated funding source for the expansion of mental health treatment options for children, adults, and seniors.

AB 1403 (Coto, 2005/2006), AB 4 (Chan, 2003/2004), and SB 1255 (Burton, 2001/2002) would have established PIT rates of 10 percent and 11 percent and increased the AMT rate for PIT taxpayers to 8.5 percent. AB 1403 failed to pass out of the Assembly Revenue and Taxation Committee; AB 4 and SB 1255 failed to pass out of the house of origin by the constitutional deadline.

SB 169 (Alquist, Stats. 1991, Ch. 117) increased the PIT rates for taxable years beginning on or after January 1, 1991, and before January 1, 1996, by adding 10 percent and 11 percent brackets and increasing the AMT rate from 7 percent to 8.5 percent.

PROGRAM BACKGROUND

For taxable years beginning on or after January 1, 1991, and before January 1, 1996, state law added PIT rates of 10 percent and 11 percent for taxable income in excess of $100,000 and $200,000, respectively.

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.

Florida does not have a personal income tax. *Illinois, Massachusetts,* and *Michigan* impose a flat tax of 3 percent, 5.3 percent, and 4.35 percent, respectively. *Minnesota* and *New York* have a progressive rate.

Minnesota has a maximum tax bracket of $74,650 for single and $131,970 for joint filers, with a maximum tax rate of 7.85 percent. *New York* has a maximum tax bracket of $500,000 for both single and joint filers, with a maximum tax rate of 8.97 percent. New York's two highest tax rates are comparable to the ones proposed by this bill.

These amounts and rates apply to returns filed in 2010 for the 2009 taxable year.

FISCAL IMPACT

This bill would require the FTB to revise the tax forms, instructions, and booklets. As a result, this bill could impact the department's printing and processing costs for tax returns. The additional costs have not been determined at this time, but will be developed as the bill moves through the legislative process.

ECONOMIC IMPACT

This bill would result in the following revenue gains:

Estimated Revenue Impact AB 1836 Effective for Taxable Years Beginning On or After January 1, 2011, and Before January 1, 2016 Assumed Enactment After September 30, 2010 ($ in Millions)		
2010/11	2011/12	2012/13
$1,100	$2,100	$2,400

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

LEGISLATIVE STAFF CONTACT

Legislative Analyst
Matthew Cooling
(916) 845-5983
matthew.cooling@ftb.ca.gov

Revenue Manager
Monica Trefz
(916) 845-4002
monica.trefz@ftb.ca.gov

Legislative Director
Brian Putler
(916) 845-6333
brian.putler@ftb.ca.gov