Franchise Tax Board

ANALYSIS OF AMENDED BILL

Author:	Calderon	Analyst:	Jahna Alvarado	Bill Number:	AB 2171
Related Bills:	See Legislative History	Telephone:	845-5683	Amended Date:	April 5, 2010
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Tax Benefits/Conditions Of Allowance

SUMMARY

This bill would limit usage of tax benefits to the allowable amount as annually determined by the State legislature, as specified.

SUMMARY OF AMENDMENTS

The April 5, 2010, amendments removed all of the bill's provisions, which related to technical changes to a provision of the Revenue and Taxation Code pertaining to the Corporate Tax Law, and replaced them with the provisions discussed in this analysis.

PURPOSE OF THE BILL

According to the author's office, the purpose of this bill is to improve the State's fiscal situation by requiring that the cost of tax benefits be accounted for within the annual State Budget.

EFFECTIVE/OPERATIVE DATE

Assuming enactment before October 1, 2010, this bill would become effective on January 1, 2011, and would be specifically operative with respect to any statute establishing a tax benefit that takes effect on or after January 1, 2011.

POSITION

Pending.

ANALYSIS

FEDERAL/STATE LAW

The Congressional Budget Act of 1974 requires that the federal budget include estimates for tax expenditures, but only for those provisions that affect the federal income taxes of individuals and corporations. The tax expenditure budget comprises the estimated revenue losses attributable to various exclusions, exemptions, deductions, nonrefundable credits, deferrals, and preferential rates in the tax code. These provisions reduce the income tax liabilities of individuals or businesses that undertake certain types of activities. For example, people who donate to charities often deduct their donations on their income tax returns and thus reduce their income tax.[1]

[1] Source: http://www.taxpolicycenter.org/briefing-book/background/expenditures/budget.cfm

Board Position:			Legislative Director	Date
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Most federal and state tax expenditures do not go through a direct appropriations process each year. Tax expenditures continue and often expand with no vote; for example, the value of charitable deductions rises with an expanding economy.

THIS BILL

This bill would condition the allowance of any tax benefit established in a State statute that becomes effective on or after January 1, 2011, to the amount that is both of the following:

- Determined by the Legislature to be consistent with the State's ability to meet its expenditure obligations under law, and
- Appropriated by the Legislature.

This bill would require that the legislative determination and appropriation occur annually.

This bill would define "tax benefit" as a credit, deduction, exclusion, exemption, or other tax advantage to a person that has the effect of reducing the person's tax liability to the state.

IMPLEMENTATION CONSIDERATIONS

The department has identified the following implementation concerns. Department staff is available to work with the author's office to resolve these and other concerns that may be identified.

The bill would make tax benefits conditional on the enactment of annual laws that would specify the amount of, and make an appropriation for, each tax benefit. Because the required action could occur at any time during a year, or not at all, this bill could create confusion and uncertainty for taxpayers and the department that would make this bill difficult to administer. For example, would the department be required to defer processing of returns until the Legislature acted? Because of the state's general conformity with federal law, would a federal law change affecting a state tax benefit be subject to Legislative action?

The bill uses the undefined term "other tax advantage to a person that has the effect of reducing the person's tax liability to the state." The absence of a definition to clarify the term could lead to disputes with taxpayers and would complicate the administration of this bill. For example, because income that is excluded from tax has the effect of reducing the tax liability (e.g., gain on the sale of a personal residence, certain retirement contributions, employer provided health benefits), this income could be included in the definition of "tax advantage."

Because tax advantages that reduce tax liability could include transactions that may not be required to be reported on a tax return (e.g., certain business reorganizations), the department could lack the information needed to identify unreported income that could become subject to tax under the terms of this bill.

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.

The laws of these states have no provisions that are comparable to this bill.

FISCAL IMPACT

The department's costs to administer this bill cannot be determined until implementation concerns have been resolved but are anticipated to be significant. Fiscal impact will be developed as the bill moves through the legislative process.

ECONOMIC IMPACT

Revenue Estimate

This bill does not change the amount of tax due under current income tax laws; therefore, there is no revenue impact.

ARGUMENTS/POLICY CONCERNS

General concepts of sound tax policy include simplicity, transparency, and certainty.[2] Taxpayers need to know that a tax exists, how to determine the tax, and how and when it is imposed on them and others. Because this bill would require annual law changes that (1) state the amount of each tax benefit that would be allowed for the year, and (2) make an appropriation for the tax benefits allowed, this bill could be in conflict with these concepts.

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[2] http://tax.aicpa.org/NR/rdonlyres/AC230E51-D650-4D65-B160-C7450A9381F4/0/2I_08a.pdf