

SUMMARY ANALYSIS OF AMENDED BILL

Author: Cook Analyst: Gail Hall Bill Number: AB 2671
 Related Bills: See Prior Analysis Telephone: 845-6111 Amended Date: June 16, 2010
 Attorney: Patrick Kusiak Sponsor: _____

SUBJECT: Minimum Franchise Tax/Exempt Corporations And Limited Liability Companies Owned Solely By Deployed Member Of U.S. Armed Forces That Operate At A Loss Or Ceases Operation

- DEPARTMENT AMENDMENTS ACCEPTED. Amendments reflect suggestions of previous analysis of bill as introduced/amended _____.
- AMENDMENTS IMPACT REVENUE. A new revenue estimate is provided.
- AMENDMENTS DID NOT RESOLVE THE DEPARTMENTS CONCERNS stated in the previous analysis of bill as introduced/amended _____.
- FURTHER AMENDMENTS NECESSARY.
- DEPARTMENT POSITION CHANGED TO _____.
- REMAINDER OF PREVIOUS ANALYSIS OF BILL AS AMENDED
- May 17, 2010, STILL APPLIES.
- OTHER – See comments below.

SUMMARY

This bill would exempt certain corporations and limited liability companies (LLCs) owned solely by a deployed member of the U.S. Armed Forces from the \$800 annual tax or minimum franchise tax.

SUMMARY OF AMENDMENTS

The June 16, 2010, amendments resolved implementation considerations No. 1 and 3 and technical consideration No. 1 (See Appendix A). Except for the “Effective/Operative Date,” and “This Bill,” discussions, the department’s analysis of the bill as amended May 17, 2010, still applies. Unresolved implementation, technical, and legal concerns are provided for convenience.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately and would apply to taxable years beginning on or after January 1, 2010, and would be specifically inoperative for taxable years beginning on or after January 1, 2018.

Board Position:	Legislative Director	Date
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<input checked="" type="checkbox"/> PENDING	Patrice Gau-Johnson	6/18/10

POSITION

Pending.

ANALYSIS

THIS BILL

This bill would allow either a corporation or an LLC that is a small business with a sole owner who is a member of the U.S. Armed Forces to be exempt from paying the \$800 minimum franchise tax (corporation) or annual tax (LLC) for any taxable year if both of the following apply:

- The owner is deployed during that taxable year, and
- The corporation operates at a loss or ceases operation in that taxable year or the LLC operation at a loss or ceases operation. (See Technical Consideration).

The Franchise Tax Board (FTB) would be required to promulgate regulations to provide for a definition of “ceases operation.”

This bill would define the following terms:

- “Deployed” would mean being called to active duty or active service during a period when a Presidential Executive order specifies that the U.S. is engaged in combat or homeland defense. “Deployed” would specifically exclude temporary duty for the sole purpose of training or processing and a permanent change of station.
- “Operates at a loss” would mean negative net income as allowed under California law.¹
- “Small business” would mean a corporation or LLC with total income of \$250,000 or less.

IMPLEMENTATION CONSIDERATIONS

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

1. This bill would require the FTB to promulgate regulations to define the term “ceases operations.” It is recommended that the author change “shall” to “may” and provide that the FTB may prescribe regulations as necessary or appropriate to carry out the purposes of this selection, including a definition for “ceases operations.”

¹ Revenue and Taxation Code (R&TC) section 24341. “Net income” means the gross income, computed under Chapter 6 (commencing with Section 24271), less the deductions allowed under this article and Article 2 (commencing with Section 24401).

TECHNICAL CONSIDERATIONS

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

The bill's reference to "the limited liability company operation at a loss" is technically incorrect because an LLC with single owner that is not classified as a corporation would not compute income or loss at the LLC "entity" level. It is recommended "operation at a loss" be revised to "operates at a loss" and the definition of "operates at a loss" is changed to "its expenses exceed its receipts.".'

LEGAL IMPACT

The bill limits the application of its provisions to a small business with "total income of \$250,000 or less." "Total income" would include worldwide income earned from within and outside of the state. The author may want to include after "total income" the phrase "from all sources derived from or attributable to the state" to limit the threshold to California receipts in order to avoid possible constitutional challenges in the future from using sources outside of the state to determine a California limitation.

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APPENDIX A
RESOLVED IMPLEMENTATION AND TECHNICAL CONSIDERATIONS

Implementation Considerations Discussed in the Department's Analysis of The Bill As Amended May 17, 2010

1. Under this bill, a member of the Armed Forces could be deployed to a location where there is no combat during a period when a Presidential Executive order specifies that the U.S. is engaged in combat or homeland defense and be permitted the benefit the bill would create. If it is the intent of the author to limit the benefit of the bill to a member of the Armed Forces deployed to a combat zone, it is recommended that the bill be amended to specify the intended limitation.
3. This bill would be specifically inoperative on January 1, 2018, which is problematic for fiscal year taxpayer's with year-ends that are different from December 31st. It is recommended that the inoperative date be revised to "taxable years beginning on or after January 1, 2018."

Technical Considerations Discussed in the Department's Analysis of the Bill as Amended May 17, 2010

1. LLC's that are not classified as corporations pay an "annual tax" instead of a "minimum franchise tax." On page 3, line 12, the author should replace "minimum franchise tax" with "the tax imposed under subdivision (a)," which reference the annual tax.