Franchise Tax Board

ANALYSIS OF AMENDED BILL

Author:	Senate Committee On Budget	Analyst:	Gail Hall	Bill Number:	SB 76
Related Bills:	See Legislative History	Telephone:	845-6111	Amended Date:	June 24, 2009
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Repeal Net Operating Loss (NOL) Carrybacks/End Assignment Of Tax Credits

SUMMARY

This bill would repeal the NOL carryback provisions and end the assignment of tax credits between members of a group.

SUMMARY OF AMENDMENTS

The provisions of this bill would make the following changes:

Provision No. 1: Remove the net operating loss carryback provisions in current law.
Provision No. 2: End the provisions that allow the assignment of tax credits.

This bill also would make changes to the Cigarette and Tobacco Products Tax Law and Oil Severance Tax Law. These changes do not affect the department and are not discussed in this analysis.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately. The operative dates of these changes vary and will be addressed separately for each provision.

POSITION

Pending.

Board Position:			Department Director	Date
_______ S	_______ NA	_______ NP		
_______ SA	_______ O	_______ NAR	Selvi Stanislaus	07/20/09
_______ N	_______ OUA	___X___ PENDING		

ECONOMIC IMPACT - SUMMARY REVENUE TABLE

Estimated Revenue Impact of SB 76 as Amended June 24, 2009 Enactment Assumed After 7/01/2009 ($ In Millions)				
Items	2009-10	2010-11	2011-12	2012-13
Provision No. 1: Repeal Carryback of NOLs	-	30	505	410
Provision No. 2: End Assignment of Tax Credit Among Affiliated Members	80	270	295	315
Interaction between NOL and tax credits provisions	-	-10	-30	-30
Total	**80**	**290**	**770**	**695**

PROVISION 1: NOL CARRYBACKS

EFFECTIVE/OPERATIVE DATE

As a tax levy, this provision would be immediately effective upon enactment and would be operative for taxable years beginning on or after January 1, 2009.

ANALYSIS

FEDERAL LAW

When a taxpayer has an operating loss for the taxable year, the operating loss that may be used in subsequent years is called a NOL. An operating loss occurs when a taxpayer's allowed deductions exceed their gross income for that year. Federal law provides, in general, that an NOL can be carried back 2 years and forward 20 years and deducted. Special rules are provided for the carryback of NOLs relating to issues such as specified liability losses, casualty or theft losses, disaster losses of a small business, and farming losses.

STATE LAW

In general, a California taxpayer calculates its NOL in accordance with federal rules. For NOLs attributable to taxable years beginning before January 1, 2008, California limits the carryforward period to 10 years in circumstances where federal law allows 20 years. For NOLs attributable to taxable years beginning before January 1, 2011, NOL carrybacks are disallowed.

NOLs attributable to taxable years beginning on or after January 1, 2008, may be carried forward 20 years. California conforms to the federal NOL carryback rules for NOLs attributable to taxable years beginning on or after January 1, 2011, with the following modifications:

1. An NOL may be carried back only 2 years. (Federal law has special rules that in some cases allow an NOL to be carried back for a longer period).
2. The amount of NOL carryback attributable to taxable year 2011 is limited to 50 percent of the NOL.
3. The amount of NOL carryback attributable to taxable year 2012 is limited to 75 percent of the NOL.

Current state law conforms to the federal carryback period for a Real Estate Investment Trust (REIT) and a corporate equity reduction interest loss, which is zero.

THIS PROVISION

This provision would remove the NOL carryback provisions under current state law.

PROVISION 2: ASSIGNMENT OF TAX CREDITS

EFFECTIVE/OPERATIVE DATE

As a tax levy, this provision would be effective immediately upon enactment and would be operative for any credit assigned by a taxpayer in taxable years beginning on or after July 1, 2008.

ANALYSIS

FEDERAL LAW

Current federal law does not permit the assignment of tax credits among taxpayers.

STATE LAW

Current state law allows the assignment of certain credits under the Corporation Tax Law to taxpayers that are members of a combined reporting group. The rules for assigning credits are included below:

- An "eligible credit" may be assigned by a taxpayer to an "eligible assignee."
  - "Eligible credit" means any credit earned by a taxpayer in a taxable year beginning on or after July 1, 2008, or any credit earned in any taxable year beginning before July 1, 2008, that is eligible to be carried forward to the taxpayer's first taxable year beginning on or after July 1, 2008.
  - "Eligible assignee" means any "affiliated corporation" that is properly treated as a member of the same combined reporting group.[1]
  - "Affiliated corporation" means a corporation that is a member of a commonly controlled group.[2]
- The election to assign any credit is irrevocable once made and is required to be made on the taxpayer's original return for the taxable year in which the assignment is made.
- The Franchise Tax Board (FTB) has authority to issue rules, procedures, guidelines and regulations necessary to implement this provision.

THIS PROVISION

This provision would end the operation of current law's assignment of credits provisions by adding an amendment that provides that a credit may be assigned only on an original return for a taxable year beginning on or after July 1, 2008, that was filed on or before the effective date of this provision.

LEGISLATIVE HISTORY

AB 1452 (Assembly Budget Committee), Stats. 2008, Ch. 763) enacted the 2-year carryback and assignment of tax credit provisions along with provisions that authorized FTB to conduct a tax amnesty (this piece was later repealed), allow an NOL carryover period of 20 years, suspend NOL deductions for two years, limit the amount of tax credits that may reduce tax for two years, and require LLCs to estimate and pay LLC fee by a specific date of the taxable year.

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.

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[1] Pursuant to R&TC section 25101 or 25110.
[2] R&TC section 25105.

NOL Carrybacks

Florida, Illinois, Massachusetts, Michigan, and Minnesota disallows NOL carrybacks, but *New York* generally follows the federal rules for NOLs but places a $10,000 limit on carrybacks.

Assignment of Tax Credits

Research found that *Florida, Illinois, Michigan, and Minnesota* have no provisions that allow for the assignment of tax credit among affiliated members.

Massachusetts law provides that for tax years beginning on or after January 1, 2009, a credit claimed by a taxable member of a combined group and that is attributable to the combined group's unitary business may be shared with the other taxable members of the combined group. The sharing of the credit must be consistent with the statutory requirement for claiming the credit, taking into account the nature of the business and activities of each of the taxable members that seek to share the credit.

FISCAL IMPACT

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

ECONOMIC IMPACT

Revenue Estimate

The revenue impact of this bill is estimated to be as shown in the following table:

Estimated Revenue Impact of SB 76 as Amended June 24, 2009 Enactment Assumed After 7/01/2009 ($ In Millions)				
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This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this bill.

Revenue Discussion

NOL Carrybacks

The revenue gain from eliminating the NOL carryback provisions is estimated with a microsimulation model. This microsimulation model combines company-level tax data on NOL availability with Department of Finance (DOF) projections for growth in business profits to project future usage of NOL carrybacks.

Use of Credits by Members of a Unitary Group

The revenue gain from disallowing the transfer of credits among affiliated corporations is estimated by using the 2005 corporate tax return sample to simulate the amount of credits that could have been transferred and applied in 2005 had the law then been in effect. In the simulation, the tax of each corporation filing a combined return with unused credits and tax liabilities greater than the minimum tax is recomputed with the assumption that unused credits may be used until either its tax is reduced to the minimum tax or the unused credit is exhausted. The simulated revenue effect of credit transfers in the 2005 taxable year is approximately $250 million. This amount is extrapolated to 2011 and later taxable years using DOF forecasts of corporate profits. Finally, the taxable-year amounts were converted to a fiscal year basis.

LEGISLATIVE STAFF CONTACT

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