Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author:	Yee/Hill	Analyst:	Matthew Cooling	Bill Number:	SBX6 21
Related Bills:	See Legislative History	Telephone:	845-5983	Introduced Date:	September 21, 2010
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Disaster Loss/San Mateo Explosion and Fire

SUMMARY

This bill would allow special tax treatment, called disaster loss treatment, for losses sustained as a result of the explosion and fire that occurred on September 9, 2010, in San Mateo County.

This analysis will not address the bill's changes to the Property Tax Law, as they do not impact the department or state income tax revenue.

PURPOSE OF THE BILL

According to the author's office, the purpose of this bill is to provide immediate tax relief to individuals and businesses affected by the explosion and fire.

EFFECTIVE/OPERATIVE DATE

As an urgency measure, this bill would be effective and operative immediately upon enactment.

POSITION

Pending.

ANALYSIS

FEDERAL/STATE LAW

Disaster Losses and Casualty Losses

Under federal law, a disaster loss is defined as business or personal property that is completely or partially destroyed as a result of a fire, storm, flood, or other natural event in an area declared to be a disaster area by the President of the United States. For state purposes, a disaster loss is defined the same as federal law but is declared to be a disaster area by the President of the United States, the Governor or both.

A casualty loss is defined as the damage, destruction, or loss of property resulting from an identifiable event that is sudden, unexpected, or unusual.

Board Position:			Department Director	Date
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Disaster Loss Treatment

Existing federal and state laws allow an individual taxpayer with a disaster loss that is not reimbursed by insurance or otherwise to deduct such losses to the extent that each loss exceeds $100 and aggregate losses for the taxable year exceed 10 percent of adjusted gross income.[1] Additionally, disaster loss treatment allows a taxpayer to make an election to claim the disaster loss by filing an amended return for the taxable year prior to the loss to receive a refund more quickly; however, this election applies automatically only to disaster losses occurring in a Presidentially-declared disaster area. The election is not available for Governor-only proclaimed disasters until enabling state legislation has been enacted.

Under existing federal law, the deadline to make an election to file an amended return is the original due date to file a return for the taxable year in which the disaster occurred.

Federal and state law also state that a casualty or disaster loss is not sustained under Internal Revenue Code section 165 until it can be ascertained with reasonable certainty whether or not a reimbursement will be received from other sources, such as insurance or an adjudicated claim.

State law must be enacted for each disaster to allow taxpayers to make the election to file a prior-year amended return, which for most individuals is by October 15th (the extended due date of the original return for the taxable year in which the disaster occurred). The extended due date for corporations varies based on each corporation's fiscal year. The election is made by the act of filing the amended return claiming the disaster loss.

State law must be enacted for each disaster, whether declared by the President or proclaimed by the Governor or both, to allow disaster losses to be carried forward (deducted) in excess of the amount that can be claimed on the prior year return or the original return for up to 15 taxable years.

Net Operating Losses (NOLs)

Under federal and state law, an NOL is created when business deductions exceed gross income. As a general rule, an individual taxpayer cannot have an NOL unless the taxpayer's return contains business deductions. A significant exception exists for casualty losses. Any deductible personal casualty loss of an individual is treated as a business deduction. Thus an individual taxpayer can have an NOL if their personal casualty loss exceeds their income.

Under federal law, an NOL may be carried back as far as two years to generate a refund. Any remaining NOL may be carried forward up to 20 years to reduce future income tax liabilities.[2]

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[1] For purposes of state income tax law, AGI is defined by cross-reference to the Internal Revenue Code (IRC) as gross income, which includes all income from whatever source derived, adjusted for certain allowable amounts, including IRA contributions, alimony paid, moving expenses, and Keogh account contributions.

[2] For federal law, if a taxpayer elects to deduct a disaster loss in the prior tax year and that deduction creates an NOL, the taxpayer can carry back the NOL to the five years preceding the year in which the taxpayer deducted the loss. An election to deduct a disaster loss in the preceding year could provide refunds for six taxable years.

California conforms to the federal NOL rules with modifications to the NOL carrybacks. Beginning on or after January 1, 2011, NOL carrybacks are allowed for two years at the following percentages:

- 50 percent for NOL carrybacks attributable to taxable year 2011.
- 75 percent for NOL carrybacks attributable to taxable year 2012.
- 100 percent for NOL carrybacks attributable to taxable year 2013.

When state legislation is enacted for disaster loss treatment, the rules for NOLs do not apply, and the taxpayer must claim their losses arising from a disaster loss using the disaster loss treatment.

PROGRAM BACKGROUND

Acting Governor Abel Maldonado proclaimed on September 10, 2010, a state of emergency declaring the explosion and fire that occurred in San Mateo County on September 9, 2010, to be a state disaster. President Obama did not declare this explosion to be a federal disaster.

<u>THIS BILL</u>

This bill would add sections to the Personal Income Tax Laws and Corporate Tax Laws under the Revenue and Taxation Code that would allow special disaster treatment of losses sustained as a result of the explosion and fire that occurred in San Mateo County on September 9, 2010.

Specifically, this bill would allow taxpayers affected by the explosion to do the following:

- Elect to file an amended return for the prior taxable year to deduct the disaster loss and reduce the prior year tax liability, resulting in a refund; and
- Allow carry forward treatment for up to fifteen taxable years for losses sustained as a result of the explosion and fire.

Losses sustained to non-business property as a result of the explosion would have to be greater than the $100 and the 10 percent of AGI limitations to qualify for disaster loss treatment.

LEGISLATIVE HISTORY

AB 50 (Nava, 2009/2010) would have allowed taxpayers disaster loss treatment for losses sustained as a result of the wildfires that occurred in Placer County during August 2009.
AB 50 failed to pass out of the Senate.

AB 1662 (Portantino, et al., Stats. 2010, Ch. 447) allows special tax treatment, called disaster loss treatment, for losses sustained as a result of the August 2009 Los Angeles and Monterey Counties wildfires and the January 2010 Calaveras, Imperial, Los Angeles, Orange, Riverside, San Bernardino, San Francisco, and Siskiyou Counties winter storms.

AB 1690 (Chesbro, Stats. 2010, Ch. 449) allows special tax treatment, called disaster loss treatment, for losses sustained as a result of the January 9, 2010, Humboldt County earthquake.

AB 1766 (Gaines, Stats. 2010, Ch. 364) allows special tax treatment, called disaster loss treatment, for losses sustained as a result of the August 2009 Placer County earthquake.

AB 1782 (Harkey, 2009/2010) would have provided automatic special tax treatment, called disaster loss treatment, for losses sustained as a result of any governor-declared state of emergency. AB 1782 was held in the Assembly Revenue and Taxation Committee.

AB 2136 (V. Manuel Perez, et al., Stats 2010, Ch. 461) allows special tax treatment, called disaster loss treatment, for losses sustained as a result of the April 2010 Imperial County earthquake.

ABX8 31 (Portantino/Jeffries, 2009/2010) would allow special tax treatment, called disaster loss treatment, for losses sustained as a result of the August 2009 Los Angeles County wildfires. ABX8 31 failed to pass prior to the adjournment of the eighth special session of 2009/2010.

FISCAL IMPACT

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

ECONOMIC IMPACT

It is assumed that all affected taxpayers will file claims and receive reimbursement from PG&E for losses sustained as a result of the explosions and fire. Therefore, there would be no deductible loss to result in a revenue impact. If it is later determined that some of the losses will not be reimbursed, the taxpayers may deduct the loss under the disaster loss rules at that time. It is expected that the revenue impact at that time would be minimal.

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