Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author:	Senate Committee On Budget and Fiscal Review	Analyst:	Gail Hall	Bill Number:	SBX8 6
Related Bills:	See Legislative History	Telephone:	845-6111	Introduced Date:	February 22, 2010
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Net Operating Loss Deduction Shall Not Exceed 68% of Taxpayer's Income/Delay Use of Assigned Credits

SUMMARY

This bill would limit the net operating loss (NOL) deduction for tax year 2010 under Personal Income Tax Law (PITL) and Corporation Tax Law (CTL), and delay by one year the operative date for the use of assigned tax credits under CTL.

This analysis will not address the bill's Education Code, Government Code, Public Utilities Code, and Streets and Highway Code provisions, as these would not impact the department or state income tax revenue.

EFFECTIVE/OPERATIVE DATE

As a special session bill, this bill would be effective 91 days after the adjournment of the special session and the 68 percent NOL limitation would be specifically operative for taxable years beginning on or after January 1, 2010, and before January 1, 2011. In addition, this bill would revise the specific operative date assigned credits may reduce tax to a taxable year beginning on or after January 1, 2011.

POSITION

Pending.

ANALYSIS

Federal Tax

When a taxpayer has a net operating loss for a taxable year, the operating loss that may be deducted in subsequent years is called an 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. For NOLs arising in taxable years ending after December 31, 2007, an eligible small business can elect to increase the NOL carryback period for an applicable 2008 or 2009 NOL from 2 years to 3, 4, or 5 years.

Board Position:			Department Director	Date
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Current federal law does not permit the assignment of tax credits among taxpayers.

State Law

NOLs

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.

Assignment of Tax Credits

Current Corporation Tax Law allows the assignment of certain credits in taxable years beginning on or after July 1, 2008, to taxpayers that are members of a combined reporting group and includes the following provisions:

- 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"[1] means any "affiliated corporation" that is properly treated as a member of the same combined reporting group.[2]
    - "Affiliated corporation" means a corporation that is a member of a commonly controlled group.[3]
- 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 FTB has authority to issue rules, procedures, guidelines, and regulations necessary to implement this provision.

[1] See R&TC section 23663(b) for the different rules on who can assign or receive credits.
[2] Pursuant to R&TC section 25101 or 25110.
[3] R&TC section 25105.

- Assigned credits may reduce tax for a taxable year beginning on or after January 1, 2010.

THIS BILL

For taxable year 2010, this bill would limit the NOL deduction as follows:

- PITL – The NOL deduction could not exceed 68 percent of "total income."
  - "Total income" would be defined gross income before any deductions allowable in determining adjusted gross income.
- CTL – The NOL deduction could not exceed 68 percent of net income.
- Any PITL or CTL NOL deduction or NOL carryover from a previous year that is disallowed due to the 68 percent limitation would have the carryover period extended by one year for the disallowed amount.

In addition, this bill would delay by one year the date that assigned credits may reduce tax. Assigned credits could reduce tax for a taxable year beginning on or after January 1, 2011.

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 the 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.

FISCAL IMPACT

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

ECONOMIC IMPACT

	The Revenue Estimate for SBX8 6 (Assumed Enactment Date before March 1, 2010) ($ in Millions)			
	2009/10	2010/11	2011/12	2012/13
Limit NOL to 68%	$ 20	$285	-$ 43	-$ 52
Delay Credit Sharing	$ 13	$240	-$ 20	-$ 20
Interaction Between Both Provisions	$ 5	$ 95	$ 56	$ 25
Total Impact	$ 38	$620	-$ 7	-$ 47

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