

ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author: Perez V. Manuel, et al. Analyst: Jahna Alvarado Bill Number: AB 1411
Related Bills: See Legislative History Telephone: 845-5683 Amended Dates: June 28 & July 12, 2011
Attorney: Patrick Kusiak Sponsor: _____

SUBJECT: Enterprise Zone Act/Modify Definitions/Modify The FTB's Reporting Requirements

SUMMARY

This bill would modify the Franchise Tax Board's (FTB's) reporting requirements under the Enterprise Zone Act.

RECOMMENDATION AND SUPPORTING ARGUMENTS

No position.

Summary of Amendments

The June 28, 2011, amendments removed the bill's provisions, which related to legislative reporting requirements with regard to geographically targeted economic development areas (G-TEDAs), and replaced them with the provisions discussed in this analysis.

The July 12, 2011, amendments added language that would limit the size of a proposed enterprise zone (EZ) in certain circumstances and make a number of technical, nonsubstantive changes. This analysis only addresses the provisions of this bill that impact the department's programs and operations.

This is the department's first analysis of this bill.

Summary of Suggested Amendments

Amendment 1 is provided to correct a punctuation error; Amendment 2 is provided to address data availability concerns; Amendment 3 is provided to eliminate inconsistent terminology; Amendment 4 would clarify language.

Amendment 5 is suggested to provide appropriation language to fund the departmental costs associated with administering this bill.

PURPOSE OF THE BILL

According to the author's office, the purpose of this bill is to improve the accountability and transparency of the state's EZ program.

Board Position:

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Executive Officer

Date

Selvi Stanislaus

8/11/11

EFFECTIVE/OPERATIVE DATE

This bill would be effective January 1, 2012, and, with respect to the provisions of the bill that affect the FTB, would apply to reports due to the Department of Housing and Community Development (DHCD) and the Legislature on or after that date.

ANALYSIS

Existing state and federal laws provide various tax credits designed to provide tax relief for taxpayers who incur certain expenses (e.g., child adoption) or to influence behavior, including business practices and decisions (e.g., research credits or economic development area hiring credits). These credits generally are designed to provide incentives for taxpayers to perform various actions or activities that they may not otherwise undertake.

STATE LAW

Under the Government Code, existing state law allows the governing body of a city or county to apply for designation as an EZ. Using specified criteria, the DHCD designates EZs from the applications received from the governing bodies. EZs are designated for 15 years (except EZs meeting certain criteria may be extended to 20 years), and the DHCD is authorized to designate 42 EZs under current law (42 are currently designated). When an EZ expires, the DHCD is authorized to designate another in its place to maintain a total of 42 EZs. The DHCD may approve the geographic expansion of EZs up to 15 percent in size and, for certain small EZs, up to 20 percent in size.

The DHCD may audit EZ programs and determine a result of superior, pass, or fail and may dedesignate failing programs. Any business located in a dedesignated zone that has elected to avail itself of any state tax incentive for any taxable year prior to dedesignation may continue to avail itself of those tax incentives for a period equal to the remaining life of the EZ, provided the business otherwise is still eligible for those incentives. When an EZ is dedesignated, it is no longer an EZ for designation purposes. Thus, when an EZ is dedesignated, the DHCD may designate another EZ in its place to maintain a total of 42 EZs.

Under the Government Code, the FTB is required to provide an annual report to the DHCD and the Legislature on the dollar value of the EZ tax incentives claimed each year by businesses operating within an EZ. Additionally, the FTB is required to develop and distribute forms to allow for the collection and reporting of the following data:

- The number of jobs for which the hiring credit is claimed;
- The number of businesses claiming each individual tax credit;
- The nature of the business claiming each individual tax credit;
- The distribution of zone tax incentives among industry groups;
- The distribution of zone tax incentives by the annual receipts and asset value of the businesses claiming each individual tax credit; and
- Any other information the FTB and the DHCD deem important in determining the costs and benefits of the EZ program to the state.

THIS BILL

Under the Government Code, this bill would, for applications for EZ designation that are submitted on or after January 1, 2012, limit the size of a proposed EZ when the proposed EZ's boundaries overlap the boundaries of one or more existing or expired EZs (previously designated EZs).

If the proposed EZ's boundary overlapped one previously existing EZ, the size of the proposed EZ would be limited to 115 percent of the size of the previously designated EZ.

If the boundary overlap involved more than one previously existing EZ, the size of the proposed EZ would be limited to 115 percent of the size of the largest previously designated EZ.

This bill would add the dollar value of "other tax-related incentives" claimed during the taxable year to the EZ information the FTB is required to collect and report. Additionally, the FTB would be required to design and distribute forms and instructions that would allow for the collection of information on the total amount of capital investments made and the total amount of the sales and use tax credit claimed by a business operating within an EZ. The number of new employees included in the computation of the hiring credit would be eliminated as a required item on forms and instructions.

Under the terms of the bill, the FTB would be required to review both personal and corporate tax returns in the development of the required information and, at minimum, report the total for each tax incentive separately for personal and corporate tax filers.

This bill would require state agencies and departments to: (1) affirmatively support their statutory responsibilities under the Enterprise Zone Act and, within their statutory responsibility, to respond to requests made by and on the behalf of an EZ, and (2) consider how the G-TEDA programs could be integrated into workforce development and training plans and strategies in order to maximize the benefits to workers and businesses.

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.

This bill uses the undefined phrase, "total amount of capital investments made." It is unclear whether "total amount" would mean tax basis or total fair market value of capital investments made (which may be different if property is acquired in a tax-deferred exchange rather than for cash). The absence of a definition to clarify this phrase could complicate the administration of this bill's reporting requirements.

It is unclear what the undefined terms “other tax-related incentives” and “tax incentive” are intended to mean. As written, the references to tax incentives could include all tax incentives granted to a business operating within an EZ, e.g., a property tax incentive offered by a local jurisdiction, and tax credits and deductions unrelated to the EZ. Expansion of the FTB’s reporting requirements beyond the EZ specific income and franchise tax incentives could significantly increase the department’s costs to produce the report. If it is the author’s intention to clarify that the report would be limited to the EZ specific income or franchise tax credits, deductions, and incentives, this bill should be amended. Suggested language is provided as Amendment 3.

The FTB utilizes a manual process to provide the EZ specific tax incentive details (as reported on the FTB Form 3805Z) on a separate basis for the approximately 5,000 corporate filers that claim EZ incentives each year. Increasing the volume of the existing manual process by approximately 23,000 Personal Income Tax (PIT) returns would significantly impact the department’s ability to provide the required report. Additionally, time limitations and resource constraints could impact the department’s ability to implement the new reporting requirements by the 2012 reporting cycle. Because of the existing data and internal processing limitations, the author may wish to amend the bill to require the FTB to report EZ tax incentive claims “to the extent that data is available.” Suggested language is provided as Amendment 2.

TECHNICAL CONSIDERATIONS

Amendment 1 is provided to eliminate a duplicate comma on page 4, line 18.

The language that would require the FTB to “review returns from personal and corporate tax returns” should be clarified. Amendment 3 is provided to change the phrase to “review tax returns filed by personal and corporate taxpayers”, which may be less confusing.

LEGISLATIVE HISTORY

AB 231 (Perez, 2011/2012) would, among other things, require state agencies to consider how the G-TEDA programs could be integrated into workforce development and training plans and strategies and would modify the FTB’s reporting requirements. The modified reporting requirements are identical to the changes that AB 1411 would make. AB 231 is currently in the Assembly Committee on Jobs, Economic Development, and the Economy.

AB 232 (Perez, 2011/2012) would, among other things, require state entities to: (1) affirmatively support their statutory responsibilities under the Enterprise Zone Act and, within their statutory responsibility, to respond to requests made by and on the behalf of an EZ, and (2) consider how the G-TEDA programs could be integrated into workforce development and training plans and strategies in order to maximize the benefits to workers and businesses. These requirements are identical to provisions of this bill. AB 232 is currently in the Assembly Committee on Jobs, Economic Development, and the Economy.

SB 301 (DeSaulnier, 2011/2012) would place a size limit on proposed EZs in certain circumstances. The limitation provision in SB 301 is identical to the limitation provision in this bill. SB 301 is currently in the Assembly Committee on Jobs, Economic Development, and the Economy.

OTHER STATES' INFORMATION

Florida, Illinois, Massachusetts, Michigan, Minnesota, and New York have zone based economic development programs. Although the law with regard to reporting on the zone based tax incentives differs among these states, a periodic reporting requirement is specified. These states were selected due to their similarities to California's economy, business entity types, and tax laws.

FISCAL IMPACT

Staff estimates costs of approximately \$133,000 in fiscal year 2011/2012 to develop, program, and test system changes necessary to implement the expanded annual reporting that this bill would require; beginning with fiscal year 2012/2013, on-going costs consist of \$128,000 to continue providing the required reports.

Due to the current fiscal environment and the redirection of resources to implement a priority technology infrastructure project, the department is unable to absorb the costs to implement the provisions of this bill. Accordingly, suggested language is provided in Amendment 5 to fund the department's implementation costs for this bill.

If this bill is enacted without appropriation language, the department would pursue a budget augmentation ("legislative budget change proposal") through the normal budgetary processes and if necessary, would redirect resources from other revenue producing activities to implement this bill. Redirection of resources could negatively impact existing revenue producing activities.

ECONOMIC IMPACT

The bill's additional reporting requirements would not impact the state's income tax revenue or the department's current programs or practices.

Modifying the Government Code provisions that govern EZ designation could affect the General Fund revenue impact of the program. For example, limiting the size of EZs proposed for designation in the future could affect the number of qualified taxpayers eligible for the various EZ income and franchise tax incentives. Because the effect, if any, would occur in the future and is impractical to predict, we are unable to provide an estimate of the revenue effect.

This analysis does not account for changes in employment, personal income, or gross state product that could result from this bill.

SUPPORT/OPPOSITION

Support: Assembly Committee on Jobs, Economic Development, and the Economy (Sponsor), California Association of Enterprise Zones.

Opposition: None provided.

ARGUMENTS

Pro: Proponents may argue that the proposed reforms to the EZ program could improve the ability of the program's stakeholders to evaluate the program's impact on economic development and job growth in the state.

Con: Opponents may argue that the proposed reforms to the EZ program could increase the program's administrative burden on state and local entities with minimal corresponding benefit.

LEGISLATIVE STAFF CONTACT

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FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO
AB 1411 AS AMENDED JULY 12, 2011

AMENDMENT 1

On page 4, line 18, strikeout "targeted tax area,," and insert:

targeted tax area,

AMENDMENT 2

On page 19, strikeout line 23, and insert:

available to the department and the Legislature information, to the extent reasonably available, by

AMENDMENT 3

On page 19, line 25, strikeout "other tax-related incentives" and insert:

zone tax incentives

AMENDMENT 4

On page 20, strikeout line 8, and insert:

shall review tax returns filed by personal and corporate taxpayers. The

AMENDMENT 5

On page 25, after line 16, insert:

SEC. 10 The sum of one hundred thirty three thousand dollars (\$133,000) is hereby appropriated to the Franchise Tax Board in augmentation of item 1730-001-0001 of the Governor's Budget, Chapter 33, Statutes of 2011. Implementation of the reporting requirements contained in section 9 of this bill is contingent upon receipt of an appropriation.