

ANALYSIS OF ORIGINAL BILL

Franchise Tax Board

Author: Cook Analyst: Jessica Matus Bill Number: AB 166
Related Bills: See Legislative History Telephone: 845-6310 Introduced Date: January 20, 2011
Attorney: Patrick Kusiak Sponsor: _____

SUBJECT: Eliminate Minimum Franchise Tax

SUMMARY

This bill would eliminate the minimum franchise tax (MFT) of \$800.

PURPOSE OF THE BILL

According to the author's office, the purpose of the bill is to stimulate business in California and make it more competitive with other states.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately upon enactment and specifically operative for taxable years on or after January 1, 2011.

POSITION

Pending.

ANALYSIS

STATE LAW

Under existing state law, unless specifically exempted by statute, every corporation organized, qualified to do business, or doing business in this state, whether organized in-state or out-of-state, is subject to the MFT. Corporate taxpayers must pay the MFT only if it is more than their measured franchise tax. In general, for taxable years beginning on or after January 1, 1997, only taxpayers subject to Corporation Tax Law with net income less than approximately \$9,040 pay the MFT because the amount of "measured" tax owed would be less than \$800 ($\$9,039 \times 8.84\% = \799).

Real estate mortgage investment conduits (REMICs) are subject to and required to pay the MFT. Regulated investment companies (RICs) and real estate investment trusts (REITs) organized as corporations are also subject to and required to pay the MFT.

Board Position:

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Department Director

Date

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02/18/11

Limited partnerships (LPs), limited liability companies (LLCs) not classified as corporations, limited liability partnerships (LLPs), and qualified Subchapter S subsidiaries (QSubs) are required to pay an annual tax equal to the MFT, but are not subject to a “measured” income tax.

Every corporation that incorporates or qualifies to do business in this state is exempt from the MFT for the first taxable year of existence. This exemption is inapplicable to any corporation that reorganizes solely for the purpose of avoiding payment of the MFT. In addition, the first-year exemption is inapplicable to the annual taxes paid by LPs, LLCs not classified as corporations, LLPs, charitable organizations, RICs, REITs, REMICs, financial asset securitization investment trusts, or QSubs.

THIS BILL

This bill would eliminate the minimum franchise tax of \$800 for all corporations for taxable years beginning on or after January 1, 2011.

IMPLEMENTATION CONSIDERATIONS

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

This bill would repeal a provision of law that requires corporations to pay the \$800 MFT. Various other types of business entities reference this provision to compute the annual tax. Eliminating the MFT provision would indirectly eliminate the annual tax for other entities that reference the repealed provision. The author may wish to amend the bill to specifically repeal only the corporate MFT, leaving the provision intact for the other business entities’ reference.

The bill would repeal the requirement to pay the MFT as of January 1, 2011. It is unclear how the bill would apply to a taxpayer whose taxable year overlaps the repeal of the MFT. For example: Taxpayer A’s year end is October 31, 2011. It is unclear if taxpayer A will be subject to the MFT. If the author’s intent is to eliminate the MFT for taxable years beginning on or after January 1, 2011, the author may wish to amend the bill to prevent disputes with taxpayers.

LEGISLATIVE HISTORY

AB 327 (Garrick, 2009/2010) would have reduced the MFT from \$800 to \$100. AB327 failed passage out of the Assembly by the constitutional deadline.

AB 1179 (Garrick, 2007/2008) would have reduced the MFT from \$800 to \$100. AB 1179 failed passage out of the Assembly Revenue and Taxation Committee.

AB 2178 (Garrick, 2007/2008) would have reduced the MFT from \$800 to \$200. AB 2178 failed passage out of the Assembly Revenue and Taxation Committee.

AB 1419 (Campbell, 1997/1998) would have reduced the MFT from \$800 to \$100. AB 1419 failed passage out of the Senate Revenue and Taxation Committee.

OTHER STATES' INFORMATION

The states surveyed include *Arizona, Florida, Illinois, Massachusetts, Michigan, Minnesota, Nevada, New York, Oregon, and Utah*. These states were selected due to their geographic proximity to California or their similarities to California's economy, business entity types, and tax laws.

Florida, Michigan, and Minnesota do not impose a minimum tax on business entities.

Arizona imposes a \$50 minimum tax on corporations.

Illinois imposes a \$25 minimum tax on corporations.

Massachusetts imposes a minimum tax of \$456 on corporations.

Nevada does not impose income tax on business entities conducting business within the state. *Nevada* does require all businesses to pay an annual "business license fee" to the Nevada Department of Taxation for the privilege of doing business within the state. For the first year an entity does business within the state, the entity is required to pay a \$200 license fee and is required to pay a \$100 license fee for each subsequent year it does business within the state.

New York imposes a minimum tax on corporations of \$25 to \$5,000 based on the corporation's in-state receipts. It also imposes a minimum tax of \$25 to \$4,500 for LPs, LLCs, and LLPs based on their in-state receipts.

Oregon imposes a \$150 minimum tax on corporations, LPs, LLCs, and LLPs.

Utah imposes a \$100 minimum tax on corporations.

FISCAL IMPACT

Implementing this bill would require some changes to existing tax forms and instructions and information systems, which could be accomplished during the normal annual update.

ECONOMIC IMPACT

Revenue Estimate

Estimated Revenue Impact of AB 166 For Taxable Years Beginning On or After January 1, 2011 Enactment Assumed After June 30, 2011 (\$ in Millions)			
2011-12	2012-13	2013-14	2014-15
-\$1,200	-\$800	-\$800	-\$850

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

LEGISLATIVE STAFF CONTACT

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