ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author:	Skinner	Analyst:	David Scott	Bill Number:	AB 2408
Related Bills:	See Legislative History	Telephone:	845-5806	Amended Date:	06/13/12
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Net Operating Loss Deduction/Disallow Carryback

SUMMARY

This bill would eliminate the two-year carryback of net operating losses (NOLs), so that NOLs could only be carried forward.

RECOMMENDATION

No position.

Summary of Amendments

The June 13, 2012, amendments removed all of the bill's provisions, which related to energy conservation, and replaced them with the provisions discussed in this analysis. This is the department's first analysis of the bill. This analysis only addresses the provisions of this bill that impact the department's programs and operations.

REASON FOR THE BILL

The reason for this bill is to eliminate the NOL carryback provisions because in the current economic situation of the State of California, the State cannot afford NOL carrybacks and these carrybacks are particularly disruptive to the State's ability to budget, and when California's most profitable companies pay less tax, the public has to pay more.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately upon enactment and operative for taxable years beginning on or after January 1, 2012.

Board Position:			Executive Officer	Date
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ANALYSIS

FEDERAL/STATE LAW

FEDERAL LAW

Federal law generally defines an NOL as the excess of deductions allowed over the gross income.

When a taxpayer has an 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 tax 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.

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 carry forward 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, 2013, 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 2013 is limited to 50 percent of the NOL.
3. The amount of NOL carryback attributable to taxable year 2014 is limited to 75 percent of the NOL.
4. The amount of NOL carryback attributable to taxable year 2015 and thereafter is 100 percent of the NOL.

Generally, no NOL deductions were allowed for taxable years 2008 through 2011. For taxable years 2008 and 2009, the deduction suspension did not apply to taxpayers with under $500,000 of net business income. For taxable years 2010 and 2011, the suspension did not apply to taxpayers with modified adjusted gross income under $300,000.

THIS BILL

This bill would remove the language in the Personal Income Tax Laws[1] and the Corporation Tax Laws[2] that allows taxpayers to carry back an NOL to the two previous taxable years and offset income from those years, resulting in a refund of taxes paid for the year(s) to which the NOL is carried back.

IMPLEMENTATION CONSIDERATIONS

Implementing this bill would not significantly impact the department's programs and operations.

LEGISLATIVE HISTORY

AB 194 (Cabellero, et. al., 2009/2010) would have repealed the NOL carryover provisions in the Revenue and Taxation Code. That bill did not pass out of the Assembly Appropriations Committee by the constitutional deadline.

AB 1936 (DeLeon, 2009/2010) would have disallowed the use of NOL carrybacks by individual and corporate taxpayers. That bill passed from the Assembly Appropriations Committee without further action.

AB 2100 (Coto, 2009/2010), as introduced on February 18, 2010, would have disallowed the use of NOL carrybacks. That bill was subsequently amended and the NOL language was removed.

SB 76 (Budget and Fiscal Review Committee, 2009/2010), as amended on June 24, 2009, would have disallowed the use of NOL carrybacks. That bill was subsequently amended and the NOL language was removed.

SB 858 (Committee on Budget and Fiscal Review, Chapter 721, Statutes of 2010), among other things, allowed an NOL deduction for NOL carrybacks for NOLs generated in taxable years beginning on or after January 1, 2013.

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.

Illinois does not conform to federal NOL rules. For corporations, partnerships, and S corporations filing in *Illinois,* there was no NOL deduction allowed for 2010-2012. No carryover deduction can exceed $100,000 for any taxable year ending on or after December 31, 2012, and prior to December 31, 2014. Any excess is carried forward for 12 years.

[1] Part 10 (commencing with Section 17001) of Division 2 of the Revenue and Taxation Code.
[2] Part 11 (commencing with Section 23001) of Division 2 of the Revenue and Taxation Code.

New York generally follows federal NOL rules, but limits the amount of the NOL carryback to $10,000. The balance of the NOL is carried forward for 20 years.

Michigan and *Minnesota* allow an NOL to be carried back for 2 years and forward for 20 years.

Florida generally follows federal NOL rules.

Massachusetts does not allow an NOL carryback and allows a five-year carry forward.

FISCAL IMPACT

Implementing this bill would not significantly impact the department's programs and operations.

ECONOMIC IMPACT

Revenue Estimate

Estimated Revenue Impact of AB 2408, as Amended on June 13, 2012 For Taxable Years Beginning On or After January 1, 2013 Enactment Assumed After June 30, 2012 ($ in Millions)				
2013/14	2014/15	2015/16	2016/17	2017/18
$5	$75	$70	$90	$90

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

SUPPORT/OPPOSITION[3]

Support: California Tax Reform Association (sponsor)

Opposition: California Chamber of Commerce
California Taxpayers Association
California Building Industry Association
California Manufacturing and Technology Association
Council on State Taxation
National Federation of Independent Business

[3] From the Senate Governance and Finance Bill Analysis, see http://www.leginfo.ca.gov/pub/11-12/bill/asm/ab_2401-2450/ab_2408_cfa_20120628_165222_sen_comm.html.

ARGUMENTS

Proponents: May say that allowing NOL carrybacks was a permanent give away for an expiring temporary stream of revenue that California cannot afford in light of its budget issues.

Opponents: May say that California's continual changes to the Revenue and Taxation Code make it difficult for taxpayers to tax plan.

LEGISLATIVE STAFF CONTACT

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