Franchise Tax Board

SUMMARY ANALYSIS OF AMENDED BILL

Author:	Quirk-Silva & Gorell	Analyst:	Diane Deatherage	Bill Number:	AB 1777
Related Bills:	None	Telephone:	845-4783	Amended Date:	May 1, 2014
		Attorney:	Bruce Langston	Sponsor:	Franchise Tax Board

SUBJECT: First-Time Abatement of Timeliness Penalties

SUMMARY

This bill would provide a penalty relief program for timeliness penalties (failure to file or failure to pay) when requested by qualified taxpayers filing under the Personal Income Tax Law and Corporation Tax Law.

RECOMMENDATION

Support.

On December 4, 2013, the three-member Franchise Tax Board voted 2-0, with the representative from Department of Finance abstaining, to sponsor the language included in this bill as introduced February 21, 2014.

SUMMARY OF AMENDMENTS

The May 1, 2014, amendments would do the following:

- Add the definition of a "qualified taxpayer," and
- Clarify refunds under the abatement program are limited by the statute of limitation for claim for refunds under current law.

As a result of these amendments, one of the technical considerations as provided in the department's analysis of the bill as amended April 7, 2014, was resolved, the department identified two additional implementation considerations and a technical consideration, and a policy concern was identified. Except for the “This Bill,” “Implementation Considerations,” “Technical Considerations,” “Economic Impact,” and “Support/Opposition” sections, the remainder of the department’s analysis of the bill as amended April 7, 2014, still applies. The Fiscal Impact section has been provided for convenience.

Summary of Suggested Amendments

Amendment language is provided to:

- Clarify the meaning of “individual taxpayer” and define the phrase “gross receipts”;
- Remove unnecessary reference to penalties assessed on partnerships and S corporations; and
- Modify the reference to provisions that would apply to overpayments and refunds.

Board Position:			Asst. Legislative Director	Date
X S	NA	NP		
SA	O	NAR	Gail Hall for	5/20/14
N	OUA		Jahna Carlson	

ANALYSIS

THIS BILL

This bill would amend state law to establish penalty abatement authority similar to the federal first-time abatement procedure.

This bill would require the Franchise Tax Board, upon a qualified taxpayer's request, to abate a failure-to-file or failure-to-pay penalty when:

- Reasonable cause is either absent or the qualified taxpayer chooses to forgo a reasonable cause review, and at the time the abatement request is made:
    - The qualified taxpayer is otherwise compliant with their income or franchise tax filing requirement;
    - For the calendar year of the request for abatement and the four years immediately prior to the request for abatement no other timeliness penalty has been imposed; and
    - The qualified taxpayer has paid, or is current on an arrangement to pay, all tax currently due.

Under this bill, “qualified taxpayer” would mean any corporation with gross receipts of less than one million dollars in the taxable year on which the timeliness penalty is imposed or an individual taxpayer.

A continuous appropriation would be made for refunds of penalties paid before the bill's effective date and abated under the bill's provisions. Such payments would constitute a public purpose.

IMPLEMENTATION CONSIDERATIONS

This bill would require changes to the department’s accounting systems to allow tracking of taxpayers that have received penalty relief based on their compliance history. Additionally, the department would require the development of procedures, training materials, notices, forms, instructions, and other documents necessary to implement the penalty relief this bill would allow.

Further, call center and accounts receivable staff estimates an increase in taxpayer requests for penalty relief and a resulting increase in the volume of “reasonable cause” determinations that would require additional staff to maintain acceptable response times.

This bill uses a phrase that is unclear, i.e., “individual taxpayer.” The absence of a definition to clarify this term could lead to disputes with taxpayers and would complicate the administration of this bill. Language is provided to clarify the meaning of the phrase in Amendment 1.

The definition of a qualified taxpayer would mean a corporation with gross receipts of less than one million dollars in the taxable year for which the timeliness penalty was imposed. It is unclear if gross receipts should be net returns and allowances, if the threshold is based on only California gross receipts, or if the gross receipts of members within a commonly controlled group are included. Amendments 2 and 3 would clarify the meaning of "gross receipts” and would be consistent with similar provisions based on gross receipts.

TECHNICAL CONSIDERATIONS

Subdivision (f) provides for a continuous appropriation from the General Fund for refund amounts of penalties abated under this bill that have been previously paid. Under existing law, these amounts would be paid from the Tax Relief and Refund Account and not the General Fund. In addition, because existing law includes a continuous appropriation to pay such amounts, this amendment is unnecessary.

Because the definition of qualified taxpayer includes only corporations and individuals, the references to the timeliness penalties assessed on partnerships[1] and S corporations[2] would have no legal effect and are unnecessary. Amendment 4 would eliminate unnecessary language.

To ensure that the relevant provisions apply regarding overpayments and refunds, it is recommended to refer to Chapter 6, instead of referring to Section 19306 specifically. Amendments 5 and 6 would ensure that all relevant overpayment and refund provisions apply to refunds of overpayments attributable to requests for abatement.

FISCAL IMPACT

Staff estimates a cost of approximately $449,000 for the systems changes, additional staffing, and development of procedures, notices, forms, instructions, and other documents necessary to implement this bill with on-going annual additional staffing costs of approximately $380,000 to address the estimated increase in taxpayer contacts resulting from this bill.

ECONOMIC IMPACT

Revenue Estimate

Estimated Revenue Impact AB 1777 As Amended May 1, 2014 Enactment Assumed After June 30, 2014 ($ in Millions)		
2014-15	2015-16	2016-17
- $5.2	- $23	- $22

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

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[1] Revenue and Taxation Code Section 19172.
[2] Revenue and Taxation Code Section 19172.5.

SUPPORT/OPPOSITION[3]

Support: Franchise Tax Board (Sponsor), California Chamber of Commerce, California Manufacturers & Technology Association, California Taxpayers Association, Spidell Publishing Inc., California Grocers Association, California Society of Enrolled Agents, Council on State Taxation, State Board of Equalization – George Runner, and State Board of Equalization – Michelle Steel

Opposition: None provided.

POLICY CONCERNS

This bill would provide a tax benefit for taxpayers who are individuals and corporations that would not be provided to other business entities. Thus, this bill would provide differing treatment based solely on classification.

LEGISLATIVE STAFF CONTACT

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[3] From the Assembly Revenue and Taxation Committee's bill analyses, dated March 21, 2014, and April 25, 2014.

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FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO AB 1777
As Amended May 1, 2014

AMENDMENT 1

On page 3, lines 3 and 4, strikeout "individual taxpayer." and insert:

individual.

AMENDMENT 2

On page 3, line 2, after "receipts" insert:

, less returns and allowances, reportable to this state

AMENDMENT 3

On page 3, between lines 4 and 5, insert:

(A) The determination of the gross receipts of a corporation, for purposes of this subdivision, shall be made by including the gross receipts of each member of the commonly controlled group, as defined in Section 25105, of which the corporation is a member.
(B) “Gross receipts, less returns and allowances, reportable to this state,” means the sum of the gross receipts from the production of business income, as defined in subdivision (a) of Section 25120, and the gross receipts from the production of nonbusiness income, as defined in subdivision (d) of Section 25120.

AMENDMENT 4

On page 3, line 6, strikeout "19131, 19132, 19172, or 19172.5." and insert:

19131 or 19132.

AMENDMENT 5

On page 3, line 20, strikeout "Subject to Section 19306, this" and insert:

This

AMENDMENT 6

On page 3, between lines 22 and 23, insert:

(5) Chapter 6 (commencing with section 19301) shall apply to refunds of overpayments attributable to requests for abatement made under this section for penalties that have been paid.