BILL ANALYSIS

Department, Board, Or Commission	Author	Provision Number
Franchise Tax Board	**Assembly Committee on Revenue & Taxation**	**AB 2754**

SUBJECT

Require Certain Business Entities e-File/ Require Dependent Tax Identification Number on Returns/Allow Credit Allocated by GO-Biz to Reduce the Tentative Minimum Tax/ Charitable Remainder Trust Conformity

SUMMARY

These provisions would do the following:

Provision 1: Require certain business entities to e-file their tax return unless a waiver is granted.

Provision 2: Provide that no Dependent Exemption Credit would be allowed unless the dependent's Taxpayer Identification Number (TIN) is included on the respective return.

Provision 3: Allow the specified tax credit allocated by the Governor's Office of Business and Economic Development (GO-Biz) to reduce tax below the tentative minimum tax.

Provision 4: Modify California tax law to conform to the federal tax treatment of charitable remainder trusts that have unrelated business taxable income.

Summary Table of Economic Impact

Estimated Revenue Impact of AB 2754 Enactment Assumed After June 30, 2014			
Description	2014-15	2015-16	2016-17
Provision 1	No impact	No impact	No impact
Provision 2	+ $10,000,000	+ $10,000,000	+ $11,000,000
Provision 3	- $400,000	- $1,300,000	- $2,200,000
Provision 4	- $450,000	- $300,000	- $300,000

PROVISION 1: REQUIRE CERTAIN BUSINESS ENTITIES TO E-FILE

REASON FOR PROVISION

The reason for this provision is to allow the department to process business entity returns more quickly, which would expedite approved refunds and utilize cost-effective technology to meet operational goals.

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EFFECTIVE/OPERATIVE DATE

This provision would be effective January 1, 2015.

Provision 1 would be specifically operative for taxable years beginning on or after January 1, 2014, for returns filed on or after January 1, 2015. The penalty would apply to acceptable returns required to be filed electronically for taxable years beginning on or after January 1, 2017.

FEDERAL LAW

The Internal Revenue Service (IRS) has an e-file system referred to as Modernized e-File (MeF). MeF is a federal web-based system that allows e-filing of corporate, individual, partnership, exempt organization, and excise returns. The IRS MeF format utilizes the same standardized technology as California's Business e-file Program. Several states that lack an e-file program participate in the Federal and State (Fed/State) program. Both the federal and state returns are transmitted to the IRS, and the IRS forwards the state return to the appropriate state tax authority.[1]

Under federal regulations, certain large corporations and other business entities are required to file federal income and information returns electronically. E-filing is optional, but encouraged, for smaller entities.

The IRS mandates e-filing for the following:

- Large corporations with $10 million or more in total assets.
- A partnership with more than 100 partners.[2] A partnership that fails to file Schedules K-1 is assessed a penalty of $50.00 for each Schedule K-1.
- Certain large tax-exempt organizations with total assets of $10 million.
- Private foundations and charitable trusts regardless of their asset size.

In addition, tax preparers that file at least 250 returns, including income tax returns, exempt organization returns, information returns, excise tax returns, and employment tax returns are mandated to e-file.

The IRS allows for exceptions and hardship waivers from the e-filing requirement. A taxpayer may request a waiver if the taxpayer is unable to meet e-filing requirements due to technology constraints or where compliance with the requirements would result in undue financial burden on the taxpayer.[3]

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[1] California is an independent state and receives state returns directly from the tax software provider, via Secure Web Internet File Transfer system, known as SWIFT.
[2] Schedules K-1.
[3] IRS Notice 2010-13.

The IRS may issue a failure-to-file penalty if a business entity chooses to file a paper return rather than e-file. A failure-to-file penalty is generally five percent of the tax owed for each month, up to a maximum of 25 percent. If the return is over 60 days late, the minimum penalty for late filing is the lesser of $135 or 100 percent of the tax owed.

STATE LAW

Current state law lacks a requirement for a business entity to e-file. The department's Business e-File Program allows business entities to voluntarily e-file returns.

State law requires income tax preparers who prepare more than 100 California individual income tax returns annually or prepare one or more using tax preparation software to e-file all personal income tax returns. The failure to e-file penalty is $50 per return unless it is shown that the failure to e-file is due to reasonable cause and not due to willful neglect.

THIS PROVISION

This provision would require that a business entity filing an acceptable return prepared using tax preparation software, must file that return by electronic technology in a form and manner prescribed by the FTB.

A business entity required to file a return electronically may annually request a waiver of the requirement from the FTB. The FTB may grant a waiver if it determines the business entity is unable to comply with the requirements due to, but not limited to, technology constraints, where compliance would result in undue financial burden, or due to circumstances that constitute reasonable cause, and not willful neglect as applicable to the penalty imposed by the provision.

This provision would define the following phrases:

- "Acceptable return" means any original return or amended return that is required to be filed, pursuant to Article 2 (commencing with Section 18601), Section 18633, Section 18633.5, or Article 3 (commencing with Section 23771) of Chapter 4 of Part 11, other than the return for unrelated business taxable income as required by Section 23771.
- "Business entity" means a corporation, including an S corporation, an organization exempt from tax, pursuant to Chapter 4 (commencing with Section 23701) of Part 11, a partnership, or a limited liability company.
- "Tax preparation software" means any computer software program used to prepare an acceptable return or for use in tax compliance.
- "Electronic technology" includes, but is not limited to, the Internet, cloud computing, or an electronic information delivery system.
- "Technology constraints" means an inability of the tax preparation software used by a taxpayer to electronically file the acceptable return as required by this section as a result of the complex nature of the return or inadequacy of the software.

This provision would apply to an acceptable return that is required to be filed on or after January 1, 2015.

Additionally, this provision would, for taxable years beginning on or after January 1, 2017, require the imposition of a $100 penalty for an initial failure and a penalty in the amount of $500 for each subsequent failure of a business entity to e-file a return, when required to do so under the requirements added by this provision, unless the failure is due to reasonable cause, and not willful neglect.

In the case of a group return filed on behalf of eligible electing taxpayer members of a combined reporting group, the penalty would apply to the combined reporting group and not to a taxpayer member of the combined reporting group.

This provision would require the FTB to conduct a robust education program advising business entities subject to the requirements of this provision of their e-filing requirement and liberally interpret and grant waivers of the penalty imposed under provisions added by the provision in order to minimize any unnecessary adverse impacts to business entities that experience difficulty complying with the new requirements.

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.

Florida law provides that a taxpayer required to e-file a federal corporate income tax return is required to file their *Florida* corporate income tax returns electronically via the IRS's MeF Fed/State Program using approved software.

Illinois and the IRS have developed the Illinois Business Income Tax MeF Program. *Illinois* requires any corporation, S corporation, and partnership that e-files its federal income tax return to file its equivalent *Illinois* income tax return for the same taxable year electronically. *Illinois* does not require e-filing of amended returns.

A *Massachusetts* S corporation that has income from customers or clients of $100,000 or more is required to e-file a corporation tax return. A *Massachusetts* partnership with 25 or more partners must e-file, and a partnership with less than 25 partners that has income or loss of $50,000 or more is required to e-file.

Michigan has an enforced e-file requirement for Michigan Business Tax (MBT) and Corporation Income Tax (CIT). All eligible MBT and CIT returns prepared using tax preparation software or a computer-generated form are required to be e-filed. *Michigan* participates in the IRS MeF Fed/State Program: accepting both MBT and CIT Fed/State e-file returns.

Minnesota accepts e-filed corporate franchise, fiduciary, S corporation, and partnership returns through participating tax software providers. *Minnesota* will begin its transition to the Fed/State MeF Program. An Internet-based e-filing platform allows a tax preparer to transmit both federal and *Minnesota* state returns through the IRS system.

New York requires a corporation and a partnership to e-file if they self-prepare tax documents without the assistance of a tax professional, utilize approved e-file tax software to prepare the return, or utilize a computer to prepare, document, or calculate an extension or estimated tax payment; and the corporation and partnership has broadband Internet access.

FISCAL IMPACT

To the extent that this provision would increase the number of taxpayers filing electronic returns versus paper, it would generate cost savings in the earlier years of implementation. The department estimates a cost savings of approximately $935,000, for fiscal year 2014-15 attributable to a reduction in personnel and equipment needed to key the business entity returns that convert from paper to e-filing and assumes that in the first year of requiring a business to e-file, a 76 percent e-file rate would be achieved. The fiscal year 2014-15 savings would be offset by a onetime implementation cost of approximately $95,000, for a net savings of approximately $840,000.

In addition, assuming achievement of a 90 percent e-file rate, approximately $510,000 in aggregate cost savings is estimated for fiscal years two through four (2015-16 through 2017-18); and cost savings in fiscal year five (2018-19) of approximately $1.2 million, by reducing work performed by vendors as the work transitions back to the department and through the elimination of maintenance support contracts. The cost savings that would result from this provision would allow staff to work higher priority workloads.

ECONOMIC IMPACT

This provision would not accelerate revenue because:

- The timing or amount of estimated tax payments made by a business entity would remain unchanged.
- The department does not prioritize e-filed returns over paper returns.
- The fact that refunds would be expected to reach taxpayers faster if they choose to e-file is estimated as having an insignificant impact on revenue.

Although this provision would impose an initial penalty of $100, increasing to $500 thereafter on a business entity that fails to e-file when required to do so, the estimated revenue associated with this penalty would be negligible because the department anticipates business entities that would be required to e-file would comply with the requirement or obtain a waiver under the provisions of the proposal. This assumption is consistent with the department’s experience with the e-file mandate for certain tax preparers preparing individual tax returns. Although certain tax preparers have been subject to the penalty, the department has been able to work with the tax preparers to either comply with the law or obtain a waiver of the e-file requirement.

APPOINTMENTS

None.

SUPPORT/OPPOSITION

Support: The Franchise Tax Board.

Opposition: None on file.

PROVISION 2: REQUIRE DEPENDENT TAX IDENTIFICATION NUMBER ON RETURNS

REASON FOR PROVISION

The reason for this provision is to allow the department to confirm that a dependent's TIN is used only once, which would increase the integrity of the returns, reduce inaccurate returns and the issuance of erroneous Dependent Exemption Credits.

EFFECTIVE/OPERATIVE DATE

This provision would be effective January 1, 2015. This provision would be specifically operative for taxable years beginning on or after January 1, 2015.

FEDERAL LAW

Under federal law, no dependent exemption is allowed unless the TIN of the dependent is included on the federal return.[4]

A TIN is an identification number used by the IRS in the administration of tax laws. The Social Security Administration issues a social security number whereas, the IRS issues all other TINs. Examples of TINs are as follows:

- Social Security Number "SSN"
- Individual Taxpayer Identification Number "ITIN"
- Taxpayer Identification Number for Pending U.S. Adoptions "ATIN"

STATE LAW

Existing state law prohibits the disallowance of the Dependent Exemption Credit if the return lacks a TIN.[5]

Additionally, state law provides that a return information notice (RIN) that includes any amount of tax that is more than the amount reported on the tax return due to a mathematical error, e.g., an inaccuracy in computation, is not a deficiency assessment and the taxpayer lacks protest or appeal rights for the adjustment shown on that RIN. However, the department may choose to collect the amount inaccurately omitted via a Notice of Proposed Assessment (NPA).[6]

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[4] Internal Revenue Code section 151(e).
[5] Revenue and Taxation Code section 17054 (d) (2).
[6] Revenue and Taxation Code section 19051.

PROGRAM BACKGROUND

In order to claim the federal dependent exemption, a taxpayer is required to provide the name and relationship of the related individual. Conversely, for each dependent exemption reported, the IRS requires the name, relationship, and, since 1987, the TIN.

Requiring the TIN has allowed the federal government to verify the dependent TIN against the social security database during return processing, and deny the dependent exemption when an inaccurate TIN is provided, or the same TIN has been reported on another return. Federal law was amended to require dependent TINs on individual tax returns because Congress viewed the TIN requirement as an enforcement mechanism for ensuring the same dependent was not claimed on multiple returns. As a result of this new requirement, seven million fewer dependent exemptions were claimed on the 1987 federal tax returns than on the 1986 federal tax returns.

Recently, the department conducted a study that confirms that failing to require the dependent TIN on the California personal income tax return (return) results in substantial noncompliance. Specific examples are situations where the same dependent is claimed three or more times on different returns, and usually this turns out to be a wholly fictitious dependent. Another common situation is where a Dependent Exemption Credit is claimed by the primary and secondary filer. The most prevalent error is the same dependent claimed exactly twice, which may indicate two parents have improperly claimed the same child, such as separated parents, or a parent has claimed their child as a dependent and that child has filed a return and claimed himself or herself.

Because state law lacks a requirement to include a dependent TIN on the return, the majority of disallowed Dependent Exemption Credits are identified when the department receives shared information from the IRS. On average, this information is received 18 months after the return's due date and includes information on the federal disallowance of dependent exemptions for failure to provide or validate the accuracy of the dependent's TIN. The remaining disallowed Dependent Exemption Credits are identified during the department's audits of the Head of Household filing status or the Child and Dependent Care Credit. Taxpayers are notified via an NPA when the Dependent Exemption Credit is proposed to be disallowed.

The department is currently implementing the Enterprise Data to Revenue (EDR) project that uses new technologies with the department's current systems with a projected goal to facilitate the validation and correction of data reported on returns through the return analysis process. This process will be performed upfront when returns are filed. If this proposal's requirement to include a dependent's TIN is enacted into law, inaccuracies identified on a taxpayer's return, such as a dependent's TIN that has been claimed on multiple returns or that do not exist, could be adjusted immediately. Requiring dependent TINs on the return would increase the department's accuracy and customer service as the adjustments could be completed at the time of return processing instead of many months later.

THIS PROVISION

This provision would, for taxable years beginning on or after January 1, 2015, provide that no Dependent Exemption Credit would be allowed unless the TIN of that individual is included on the return claiming the credit. Any disallowance of the Dependent Exemption Credit due to the omission of a TIN would be treated as a math error by the department. A taxpayer would have the right to subsequently provide the TIN and receive a credit or refund if provided prior to the expiration of the statute of limitations.

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.

Florida only has a corporation income tax; therefore, a comparison with *Florida* law is irrelevant.

Generally*, Illinois* does not require a TIN to be reported on the return in order to claim a dependent exemption. However, a Nonresident Alien is required to attach the federal 1040 NR or 1040 NR-EZ when filing the state return.

Massachusetts has a Dependent Information Schedule that requires the dependent's name, relationship, TIN, and date of birth.

Michigan does not require a TIN to be reported on the return or an attached federal return in order to claim a dependent exemption.

Minnesota has a Child and Dependent Care Credit Schedule, Minnesota Working Family Credit Schedule, and a K-12 Education Credit Schedule that requires, among other information, the dependent's name, TIN, and date of birth.

New York requires a dependent's name, relationship, TIN, and date of birth to be reported on the return in order to claim the dependent exemption.

FISCAL IMPACT

This provision would require the department to respond to and resolve taxpayer contacts when their Dependent Exemption Credit has been disallowed resulting in additional costs of approximately $512,000 for the first year (2014-15), and $504,000 for each subsequent year. Any costs attributable to system changes are expected to be absorbable.

ECONOMIC IMPACT

Revenue Estimate

Estimated Revenue Impact of AB 2754 Provision 2 Enactment Assumed After June 30, 2014 ($ in Millions)		
2014-15	2015-16	2016-17
+ $10	+ $10	+ $11

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

Revenue Discussion

Each year approximately 12 million dependent exemption credits are claimed on 7.6 million personal income tax returns. Based on an internal study, approximately 65,000 dependent exemptions on these returns are expected to be disallowed because of duplicate or missing TINs. Of the total exemptions disallowed, approximately 15 percent would ultimately be accepted because the taxpayer correctly claimed the dependent exemption credit. Given an average tax impact of $209 per return, the remaining 85 percent or approximately 55,000 returns would result in savings of approximately $11,000,000 in the first year. However, a small portion of this savings, or approximately $850,000, will not be paid timely. It is estimated that 60 percent of the $850,000 will be collected over the next 5 years. The result is a total annual savings of approximately $10,000,000 in fiscal year 2015-16. Standard growth and fiscalization rates were applied.

APPOINTMENTS

None.

SUPPORT/OPPOSITION

Support: Franchise Tax Board.

Opposition: None on file.

PROVISION 3: INCLUDE THE SPECIFIED TAX CREDIT ALLOCATED BY GO-BIZ AS A CREDIT ALLOWED TO REDUCE TAX BELOW THE TENTATIVE MINIMUM TAX.

REASON FOR PROVISION

The reason for this provision is to allow taxpayers to fully utilize the GO-Biz California Competes Credit by allowing the credit to reduce the tentative minimum tax (TMT).

EFFECTIVE/OPERATIVE DATE

This provision would be effective January 1, 2015.

This provision would be specifically operative for taxable years beginning on or after January 1, 2014.

FEDERAL LAW

General business credits allowed for any tax year are limited to the excess of a taxpayer's “net income tax” over the greater of: (1) the tentative minimum tax for the tax year, or (2) 25 percent of the amount of the taxpayer's “net regular tax” that exceeds $25,000. In addition, the empowerment zone employment credit, the New York Liberty Zone business employee credit, “specified credits,” and eligible small business credits have various rules for limiting the usage of credits[7].

STATE LAW

Under state law, the general rule is that tax credits imposed under the Personal Income Tax Law (PITL) or the Corporation Tax Law (CTL) may not reduce regular tax below TMT, unless specifically provided otherwise.

THIS PROVISION

This provision would allow the California Competes Credit to reduce the regular tax below tentative minimum tax under the PITL and CTL for taxable years beginning on or after January 1, 2014.

In addition, this provision provides double jointing[8] language that would prevent this provision and AB 1839 from chaptering out[9] section 23036 of the Revenue and Taxation Code that is amended in each provision.

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.

Florida and *Minnesota* impose corporate TMT; *Illinois, Massachusetts, Michigan,* and *New York* do not.

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[7] IRC section 38(c).

[8] *Double* jointing refers to technical amendments necessary when two or more bills propose to amend the same code section (i.e., Revenue & Taxation Code Section 23036). Double jointing prevents the problem of chaptering out.

[9] Chaptering out means when, during a calendar year, two or more bills amending the same code section become law, and the bill enacted last (with a higher chapter number) becomes law and prevails over the code section in the previously enacted.

FISCAL IMPACT

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

ECONOMIC IMPACT

Revenue Estimate

Estimated Revenue Impact of AB 2754 Provision 3 Enactment Assumed After June 30, 2014		
2014-15	2015-16	2016-17
- $400,000	- $1,300,000	- $2,200,000

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

Revenue Discussion

Based on an analysis of recent returns of taxpayers that have been chosen by GO-Biz to receive these credits, the FTB estimates that allowing taxpayers to use GO-Biz credits to offset regular tax below TMT would result in an additional estimated revenue loss of $400,000 in the first year.

It is assumed that as GO-Biz continues to allocate credits over the next four years the amount of additional credit available for use against TMT would increase proportionally to the credits allocated. However, it is important to note that the amount of credits allowed under this provision would have the effect of reducing the amount of credits claimed in future years.

APPOINTMENTS

None.

SUPPORT/OPPOSITION

Support: None on file.

Opposition: None on file.

PROVISION 4: MODIFY CALIFORNIA TAX LAW TO CONFORM TO THE FEDERAL TAX TREATMENT OF CHARITABLE REMAINDER TRUSTS THAT HAVE UNRELATED BUSINESS TAXABLE INCOME.

REASON FOR PROVISION

The reason for the provision is to allow charitable remainder trusts that have unrelated business taxable income to retain their tax-exempt status on other trust income.

EFFECTIVE/OPERATIVE DATE

This provision would be effective January 1, 2015. This provision would be specifically operative for taxable years beginning on or after January 1, 2014.

FEDERAL/STATE LAW

Under federal and state law, a charitable remainder trust is generally a trust that:

- Is funded by a donor's irrevocable contribution of cash or property,
- Provides the donor, other designated beneficiaries, or both, an income stream for a specified period, commonly for the life of one or more beneficiaries, and
- Contributes the remainder of the trust to charity.

The remainder to be contributed to charity must be at least ten percent of the value of the assets contributed to the trust, and the donor is allowed a charitable contribution deduction in the year of the contribution for the present value of the remainder.

A charitable remainder trust is generally tax exempt; that is, income that would otherwise be currently taxable as trust income is generally not taxable until it is distributed to a beneficiary, unless the trust has unrelated business taxable income.[10] If a charitable remainder trust has unrelated business taxable income in any taxable year, then:

- For federal purposes, the charitable remainder trust retains its general tax-exempt status for that taxable year, but is subject an excise tax equal to the amount of unrelated business taxable income; and
- For California purposes, the charitable remainder trust loses its tax-exempt status for that taxable year and is taxed on its income.

This differing treatment between federal and state law is due to a 2006 federal tax law change to which California specifically does not conform. In the Tax Relief and Health Care Act of 2006 (TRHCA), the federal tax rules that apply to a charitable remainder trust with unrelated business taxable income were changed as follows:

Pre-TRHCA Federal Rules

Prior to the TRHCA, the federal rules were generally the same as the current California rules; that is, for taxable years beginning before January 1, 2007, a charitable remainder

[10] Unrelated business taxable income generally is the income from a trade or business regularly conducted by an exempt organization and not substantially related to the performance by the organization of its exempt purpose or function, except that the organization uses the profits derived from the activity. Common types of charitable remainder trust unrelated business taxable income include an investment in an active trade or business (e.g., a partnership or limited liability company interest), a working interest in an oil and gas well, and unrelated debt-financed income from trading on the margin or other borrowing.

trust with unrelated business taxable income in any taxable year lost its tax-exempt status for that year, and the charitable remainder trust was taxed as a regular complex trust. As such, the trust was allowed a deduction in computing taxable income for amounts required to be distributed in a taxable year, not to exceed the amount of the trust's distributable net income for the year.

This rule was applied on a year-by-year basis; that is, a charitable remainder trust with unrelated business taxable income lost its general tax exemption for the year, but such trust would continue to be tax exempt in subsequent years in which it had no unrelated business taxable income.

Post-TRHCA Federal Rules

The TRHCA provides that for taxable years beginning on or after January 1, 2007, a 100-percent excise tax is imposed on the unrelated business taxable income of a charitable remainder trust. This replaces the rule that took away the income tax exemption of a charitable remainder trust for any taxable year in which the trust had any unrelated business taxable income.

California generally conforms to the federal rules for charitable remainder trusts, but specifically does not conform to the 2006 TRHCA change described above. Thus, for California purposes, a charitable remainder trust that has unrelated business taxable income in any taxable year loses its general exemption from income tax for that year and is taxed as a regular complex trust.

Similar to the federal law prior to the TRHCA, the unrelated-business-taxable-income rule is applied on a year-by-year basis under California law; that is, a charitable remainder trust with unrelated business taxable income loses its general tax exemption for the taxable year, but such trust continues to be tax exempt in subsequent years in which it has no unrelated business taxable income.

THIS PROVISION

This provision would conform California law to the current federal rules applicable to charitable remainder trusts that have unrelated business taxable income, modified to provide that in lieu of a 100-percent excise tax on unrelated business taxable income, California unrelated business taxable income would be subject to tax under the graduated personal income tax rates that range from 1 percent to 13.3 percent.[11]

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[11] R&TC sections 17041 and 17043. Proposition 30, passed by a majority of California voters on November 6, 2012, added Section 36 to Article XIII of the California Constitution, which temporarily increases the top tax rate of 9.3 percent under R&TC section 17041. For taxable years beginning on or after January 1, 2013, and before January 1, 2019, the 9.3 percent tax rate is increased for taxpayers that have taxable income over $250,000. The increased tax rates are 10.3 percent for the portion of taxable income that is over $250,000 but not over $300,000, 11.3 percent for the portion of taxable income that is over $300,000 but not over $500,000, and 12.3 percent for the portion of taxable income that is over $500,000. R&TC section 17043 imposes a one-percent additional tax on the portion of a taxpayer's taxable income in excess of $1,000,000.

LEGISLATIVE HISTORY

SB 401 (Wolk, Chapter 14, Statutes of 2010) changed California's "specified" date of conformity to the Internal Revenue Code from January 1, 2005, to January 1, 2009, and modified California law to specifically not conform to the charitable remainder trust rule changes relating to unrelated business taxable income that were made by the TRHCA.

AB 2687 (Assembly Committee on Revenue and Taxation, 2011/2012) would have, similar to this provision, conformed to the federal treatment of charitable remainder trusts with unrelated business taxable income. AB 2687 failed to pass.

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. A review of the laws of these states found that none revoke a charitable remainder trust's general tax-exempt status in any year the trust has unrelated business taxable income.

FISCAL IMPACT

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

ECONOMIC IMPACT

Revenue Estimate

Estimated Revenue Impact of AB 2754 Provision 4 Assumed Enactment After June 30, 2014		
2014-15	2015-16	2016-17
- $450,000	- $300,000	- $300,000

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

Revenue Discussion

This estimate is based upon a proration of the Joint Committee on Taxation (JCT) estimate for this provision when it was enacted for federal purposes in 2006.

The JCT estimates the revenue impact of the federal provision to be a loss of $8 million in fiscal year 2014-15. An economic adjustment factor of approximately 93 percent is first applied to the federal estimate to account for changes in the growth between 2006 and 2014. A proration ratio of approximately 3.8 percent is then applied to account for California's share of the national economy, differences between California and federal personal income taxation rates, and differences in the proposed law. Using this method, the department estimates a loss of approximately $280,000 in the 2014 taxable year.

Because the operative date would be January 1, 2014, and the enactment date would be after June 30, 2014, the revenue impact for all of taxable year 2014 will fall in fiscal year 2014-15. Fiscalization of the remaining taxable years is split between fiscal years, as reflected in the table above.

SUPPORT/OPPOSITION

Support: None on file.

Opposition: None on file.

VOTES

	Date	Yes	No
Concurrence	08/28/14	54	24
Senate Floor	08/26/14	24	12
Assembly Floor	05/29/14	55	20

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