Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author:	Gaines	Analyst:	Davi Milam	Bill Number:	SB 31
Related Bills:	See Legislative History	Telephone:	845-2551	Introduced Date:	December 1, 2014
		Attorney:	Bruce Langston	Sponsor	

SUBJECT:	Personal Exemption Credit/Increase to $652 for Each Dependent

SUMMARY

Under the Personal Income Tax Law (PITL), this bill would increase the dependent exemption credit to $652 per dependent.

RECOMMENDATION

No position.

Summary of Suggested Amendments

Amendments 1 through 4 are suggested to resolve a technical concern.

REASON FOR THE BILL

The reason for this bill is to increase the take-home pay of working families.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2015.

FEDERAL/STATE LAW

Overview

Federal and state law both provide “personal-exemption” type reductions to tax; however, federal law provides a “personal-exemption” deduction, whereas the state provides “personal-exemption” tax credits. An exemption deduction is a reduction to adjusted gross income to arrive at taxable income, whereas a tax credit is a dollar-for-dollar reduction to tax.

Board Position:						Executive Officer	Date
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Federal Law

Federal law provides a "personal-exemption" deduction.[1] Taxpayers are generally allowed one personal exemption for themselves, and an exemption for each claimed dependent. Each exemption is worth the same amount, and taxpayers multiply the total number of exemptions by the current-year exemption amount. The exemption deduction is $3,950 for taxable year 2014, and is adjusted annually based on the Consumer Price Index published by the Department of Labor. In addition to the personal exemptions, federal law also provides exemption deductions for senior, blind, and disabled taxpayers.

The exemption deduction is reduced if a taxpayer's federal adjusted gross income (AGI) exceeds the applicable amount. The applicable phase-out amounts are adjusted annually based on the Consumer Price Index published by the Department of Labor.

Each dependent's taxpayer identification number (TIN) must be provided on the federal tax return or the dependent exemption will be disallowed.

State Law

State law provides various exemption credits, including a personal exemption credit and exemption credits for dependents, blind persons, and individuals 65 or older. Unlike federal law, these exemptions are not deductions from AGI but are credits against tax. The exemption credit amounts for the 2014 taxable year are $333 per dependent and $108 per all other exemptions.

The exemption credit amounts are indexed annually for inflation. The exemption credits are not refundable and may not be carried over to future years. Exemption credits begin to phase out at federal AGI levels in excess of the amounts listed below:

Filing Status	AGI (2014)
Single/Married/RDP Filing Separate	$176,413
Head of Household	$264,623
Married Filing Joint/Qualifying widow(er)	$352,830

The exemption credit amount is reduced by $6 for every $2,500 ($1,250 for married filing a separate return) that the taxpayer's federal AGI exceeds the above threshold amounts, not to exceed the full amount of the credit. Taxpayers who file a joint return or who file as a surviving spouse must reduce their credit by $12 for every $2,500.

For taxable years beginning on or after January 1, 2015, the dependent's TIN must be provided on the California tax return or the dependent exemption credit will be disallowed.

[1] IRC section 151.

THIS BILL

For taxable years beginning on or after January 1, 2015, this bill would increase the dependent exemption credit amount from $333[2] to $652 per dependent.

For taxable years beginning on or after January 1, 2016, the increased dependent exemption amount in this bill would be indexed for inflation.

The increased credit amounts would continue to be subject to AGI limitations.

IMPLEMENTATION CONSIDERATIONS

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.

TECHNICAL CONSIDERATIONS

Amendments 1 through 4 are provided to correct a cross-referencing error that inadvertently eliminates the requirement to provide each dependent's TIN.

LEGISLATIVE HISTORY

ABX1 18 (Blumenfield, 2011/2012) would have continued the decrease in the dependent exemption credit to the same amount as the personal exemption credit for taxable years 2011 and 2012. This bill failed to pass out of the Senate by the constitutional deadline.

ABX3 3 (Evans, Chapter 18, Statutes of 2009) decreased the dependent exemption credit to the same amount as the personal exemption credit amount for taxable years 2009 and 2010.

SB 952 (Wyland, 2009/2010) and AB 1700 (Gaines, 2009/2010) would have repealed the reduction of the dependent exemption credit enacted in 2009, and for taxable years beginning on or after January 1, 2010, would have increased the dependent exemption credit amount to the amount it would have been if the reduction had never become operative. Both bills failed to pass by the constitutional deadline.

AB 2797 (Cardoza, et al., Chapter 322, Statutes of 1998) changed the amount of the dependent exemption credit for taxable years 1998 and 1999, and required the new amounts to be indexed for inflation thereafter.

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[2] The dependent exemption credit amount of $333 reflects the base credit of $227 adjusted for inflation pursuant to R&TC section 17054.

OTHER STATES' INFORMATION

The states surveyed include *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 allows an exemption deduction for taxpayers and their qualifying dependents. For tax year 2013, the exemption amount was $2,100.

Massachusetts allows a $1,000 exemption deduction for each dependent claimed on the taxpayer's federal income tax return.

Michigan allows an exemption deduction of $3,950 for the taxpayer, the taxpayer's spouse, and each dependent.

Minnesota allows a $3,900 exemption deduction for each dependent claimed on the taxpayer's federal income tax return.

New York allows a $1,000 exemption deduction for each dependent.

FISCAL IMPACT

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

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue losses:

Estimated Revenue Impact of SB 31 As Introduced December 1, 2014 Assumed Enactment After June 30, 2015 ($ in Billions)		
2015-16	2016-17	2017-18
- $2.2	- $1.4	- $1.5

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

Revenue Discussion:

This estimate is based on output from the department's personal income tax micro-simulation model. The model projects the aggregate amount of dependent credits claimed for future years on the basis of the number of dependents claimed in prior years and the amount of credit per dependent under the current and proposed laws. The model then calculates the revenue impacts as the difference in the aggregate tax liabilities under the current and proposed laws. The tax year estimates are then converted to fiscal year estimates and reflected in the table above.

SUPPORT/OPPOSITION

Support: None provided.

Opposition: None provided.

ARGUMENTS

Proponents: Supporters may argue that this bill would increase the disposable income of California's working families and enhance the state's economic recovery.

Opponents: Some may argue that this bill should be broadened to increase the personal exemption credit in an effort to assist all California taxpayers rather than only those taxpayers with dependents.

LEGISLATIVE STAFF CONTACT

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FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO SB 31
As Introduced December 1, 2014

AMENDMENT 1

On page 2, line 13, after "(1)" insert:

(A)

AMENDMENT 2

On page 2, line 22, strikeout "(2)" and insert:

(B)

AMENDMENT 3

On page 2, line 31, strikeout "(3)" insert:

(2)

AMENDMENT 4

On page 3, line 5, strikeout "(4)" and insert:

(3)