BILL ANALYSIS

Department, Board, Or Commission	Author	Bill Number
Franchise Tax Board	**Wolk & Dodd**	**SB 35**

SUBJECT

Disaster Loss Deduction/Automatic Disaster Relief for Areas Proclaimed by Governor to be in State of Emergency

SUMMARY

This bill would, under the Personal Income Tax Law and the Corporation Tax Law, automatically allow disaster loss treatment for losses sustained in an area declared by the Governor to be in a state of emergency.

REASON FOR THE BILL

The reason for the bill is to streamline the disaster tax relief process, reduce the burden of multiple disaster loss bills on the Legislature, and to expedite disaster-related tax relief for taxpayers that suffer losses related to governor-declared states of emergency.

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, 2014, and before January 1, 2024.

FEDERAL/STATE LAW

Under federal and state law, a disaster loss occurs when business or personal property is completely or partially destroyed as a result of a fire, storm, flood, or other natural event.

Internal Revenue Code (IRC) section 165(i), allows a taxpayer that suffers a disaster loss to elect to deduct the loss in the year immediately preceding the year the disaster occurred if it is a Presidentially-declared disaster loss.

Similarly, California law conforms to IRC section 165(i) allowing taxpayers to elect to file an amended return to deduct a disaster loss in the taxable year prior to the loss year, for any Presidentially-declared disaster. The election is not available for a Governor-only declared disaster area until enabling state legislation has been enacted.

Existing federal and state law allows an individual taxpayer with a disaster loss that is not reimbursed by insurance or otherwise, to deduct disaster losses to the extent that each loss exceeds $100 and aggregate net losses for the taxable year exceed 10 percent of adjusted gross income. Business and income-producing property are not subject to these limitations.

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Date
8/19/15

If a disaster loss deduction creates a net operating loss, the carry forward treatment and carryback treatment apply.

State Net Operating Loss (NOL) Carryback Rules

Beginning on or after January 1, 2013, NOLs must be carried back to each of the preceding two taxable years, unless an election to waive the carryback is made. Any excess loss may be carried forward for 20 years starting with the tax year that generated the loss. The NOL carryback may not be carried back to a tax year beginning before January 1, 2011. The allowable NOL carryback percentage increases during a phase-in period, which varies by the loss year, as shown in the table below:

NOL Incurred in Tax Year[1]	NOL Carryback Percentage
2015 and after	100%
2014	75%
2013	50%

PROGRAM BACKGROUND

Generally, the governor has authority to proclaim a state of emergency declaring certain natural disasters, (i.e., wildfires, mudslides, floods, and severe winter storms) to be a state of emergency. Upon declaration of a state of emergency, the Legislature can propose special tax treatment, called disaster loss treatment, for taxpayers affected by a governor-declared emergency.

THIS BILL

For taxable years beginning on or after January 1, 2014, and before January 1, 2024, this bill would allow a taxpayer to elect disaster loss treatment under IRC Section 165(i) for any loss sustained in any city, county, or city and county in California that is proclaimed by the Governor to be in a state of emergency.

This bill would provide that an IRC Section 165(i) election relating to disaster losses could be made on a return or amended return filed on or before the due date of the return (including the extended due date) for the taxable year in which the disaster occurred.

Additionally, this bill would preclude any law, other than those specific to NOL treatment under the R&TC,[2] that suspends, defers, reduces, or otherwise diminishes the deduction of an NOL from applying to an NOL attributable to a loss sustained in any city, county, or city and county in California that is proclaimed by the Governor to be in a state of emergency.

This bill would be repealed by its own terms as of December 1, 2024.

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[1] Pursuant to Revenue and Taxation Code (R&TC) sections 17276.20 & 24416.20.
[2] R&TC sections 17276.20 and 24416.20.

LEGISLATIVE HISTORY

AB 1782 (Harkey, 2009/2010), similar to this bill, would have provided disaster loss treatment for losses sustained as a result of any governor-declared state of emergency. AB 1782 failed to pass out of the Assembly Revenue and Taxation Committee by the constitutional deadline.

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 does not have a personal income tax; however, monetary relief is provided to citizens and corporations through the Emergency Management, Preparedness, and Assistance Trust Fund. Florida also requires legislation, executive order, or proclamation to identify the area impacted by a disaster.

Illinois, *Massachusetts*, *Michigan*, *Minnesota*, and *New York* conform to the federal provisions that allow taxpayers to claim a disaster loss deduction on their state tax returns either in the preceding year or in the year of the loss. It appears that legislation, executive order, or proclamation by the President or the Governor is required to identify the area impacted by a disaster that is eligible for federal or state assistance.

FISCAL IMPACT

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

ECONOMIC IMPACT

Revenue Estimate:

The revenue impact associated with this disaster bill is primarily attributable to timing differences and therefore, the net revenue loss is minimal.

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

Revenue Discussion:

The revenue impact of this bill depends on the extent affected taxpayers elect to claim their disaster loss by either amending their preceding year return or waiting to claim the disaster loss when filing their current year return. The revenue impact of this bill is primarily attributable to the timing difference between these two options for claiming the disaster loss. Because it is assumed a taxpayer would choose the disaster loss reporting option that is the most beneficial to their financial situation, it is estimated that there would be a small revenue loss. Historically, the department has estimated the revenue impact of disaster losses to be approximately $1,000 per disaster.

APPOINTMENTS

None.

SUPPORT/OPPOSITION

Support: None provided.

Opposition: None provided.

VOTES

	Date	Yes	No
Concurrence	08/17/15	38	0
Assembly Floor	07/16/15	79	0
Senate Floor	04/09/15	38	0

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