ANALYSIS OF AMENDED BILL

Author:	Gaines	Analyst:	Funmi Obatolu		Bill Number:	SB 874
Related Bills:	See Legislative History	Telephone:	845-5845	Amended Date:		March 15, 2016
		Attorney:	Bruce Langston	Sponsor		

SUBJECT: Personal Exemption Credit /Increase to $422 for Each Dependent

SUMMARY

Under the Personal Income Tax Law, this bill would modify the dependent exemption credit for dependents.

RECOMMENDATION

No position.

Summary of Amendments

The March 15, 2016, amendments removed provisions of the bill related to the Public Utilities Code and replaced them with the provisions discussed in this analysis.

This is the department's first analysis of the bill.

Summary of Suggested Amendments*

Amendments 1 through 6 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, 2016.

FEDERAL/STATE LAW

Overview

Federal and state laws 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.

Federal Law

Under Federal law 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 $4,000 for taxable year 2015, and is adjusted annually based on the Consumer Price Index published by the Department of Labor (CPI). 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 CPI.

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 2015 taxable year are $337 per dependent and $109 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:

Filling Status	AGI (2015)
Single/Married /RDP Filling Separate	$178,706
Head of Household	$268,063
Married Filing Joint/Qualifying widow(er)	$357,417

The exemption credit amount is reduced by $6 for every $2,500 ($1,250 for married taxpayers 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.

THIS BILL

For taxable years beginning on or after January 1, 2016, this bill would increase the dependent exemption credit amount from $337 to $422 per dependent.

For taxable years beginning on or after January 1, 2017, the increased dependent exemption amount would be indexed for inflation.

IMPLEMENTATION CONSIDERATIONS

Implementing this bill would require changes to existing tax forms and instructions and information systems.

TECHNICAL CONSIDERATIONS*

Amendments 1 through 6 are provided to correct a cross-referencing error that inadvertently eliminates the requirement to provide each dependent's TIN.

LEGISLATIVE HISTORY

SB 31 (Gaines, 2015/2016) would have increased the dependent exemption credit to $652 per dependent. SB 31 failed to pass by the constitutional deadline.

ABX1 18 (Blumenfield, 2011/2012) would have decreased the dependent exemption credit to the same amount as the personal exemption credit for taxable years 2011 and 2012. ABX1 18 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.

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.

Illinois allows an exemption deduction for taxpayers and their qualifying dependents. For tax year 2015, the exemption amount was $2,150.

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 $4,000 for the taxpayer, the taxpayer's spouse, and each dependent.

Minnesota allows a $4,000 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

The department's costs to implement this bill have yet to be determined. As the bill moves through the legislative process, costs will be identified and an appropriation will be requested, if necessary.

ECONOMIC IMPACT

This bill would result in the following revenue loss:

Estimated Revenue Impact of SB 874 As Amended March 15, 2016 Assumed Enactment After June 30, 2016 ($ in Millions)		
2016-17	2017-18	2018-19
- $390.0	- $410.0	- $420.0

Revenue Discussion

The estimated revenue impact of increasing the dependent exemption credit was computed using a two step analysis. First, the $337 dependent exemption credit from taxable year 2015 was grown using the California Consumer Price Index (CPI) for 2016, resulting in an estimated dependent exemption credit of $343. This amount and the indexed amounts for each year thereafter were run through the department's Personal Income Tax (PIT) simulation model to calculate the tax impact of the credit under current law. Next, the proposed $422 credit amount and the indexed amounts for the credit were run through the PIT simulation model to calculate the tax impact of the proposed credit. The current law amounts were subtracted from the proposed law amounts resulting in the taxable year 2016 estimated tax impact of $390 million.

The tax year estimates were converted to fiscal years, and rounded to arrive at the amounts reflected in the above table.

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 874
As Introduced March 15, 2016

AMENDMENT 1

On page 2, line 20, after "(1)" insert:

(A)

AMENDMENT 2

On page 2, line 25, strikeout "paragraph" insert:

Subparagraph

AMENDMENT 3

On page 2, line 29, strikeout "(2)" insert:

(B)

AMENDMENT 4

On page 2, line 34, strikeout "paragraph" insert:

subparagraph

<center>AMENDMENT 5</center>

On page 3, line 1, strikeout "(3)" insert:

(2)

<center>AMENDMENT 6</center>

On page 3, line 15, strikeout "(4)" insert:

(3)