

ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author: Runner Analyst: Colin Stevens Bill Number: AB 24

Related Bills: See Legislative History Telephone: 845-3036 Amended Date: 4/15/99

Attorney: Patrick Kusiak Sponsor: _____

SUBJECT: Bank Tax Rate Excess Over General Tax/Local Agency Financial Aid Fund/In-lieu Provisions Don't Pertain To Real Property Or Certain Parcel Taxes

SUMMARY OF BILL

This bill would make the following changes to the in-lieu tax applicable to banks and financial corporations:

- require that the revenues from the in-lieu tax be deposited into the Financial Aid to Local Agencies Fund (the Fund), which would be created by the bill, for disbursement by the Controller to cities, counties and cities and counties based on a formula to be prescribed by the Legislature;
- require the FTB to notify the Controller semiannually of the amount of collected taxes attributable to the bank tax; and
- specify that the tax would not be in-lieu of nondiscriminatory parcel taxes.

SUMMARY OF AMENDMENT

The April 15, 1999, amendments removed the bill's prior provisions and inserted the provisions discussed in this analysis.

EFFECTIVE DATE

The provisions of this bill relating to the Fund would apply beginning with the 2000-2001 fiscal year. The nondiscriminatory property tax provision would apply to income years beginning on or after January 1, 1999.

LEGISLATIVE HISTORY

AB 3212 (1995/96) and AB 511 (1997/98) both would have transferred revenues from the in-lieu rate to cities; both failed passage.

PROGRAM HISTORY

Under prior federal law, states were allowed to tax federally chartered (national) banks only by using one of four methods: 1) taxing bank shares; 2) including bank share dividends in the taxable income of a shareholder; 3) taxing national banks on their net income; or 4) levying a non-discriminatory franchise tax on national banks according to or measured by their net income.

California law adopted the fourth option by means of the bank tax, which consists of the corporate franchise tax and the "in-lieu" tax. **Under state law**, national banks, state-chartered banks, and financial corporations are exempted from personal property and certain other local taxes and instead are subject to the franchise tax and to a special in-lieu tax measured by net income.

Board Position:	Department Director	Date
_____ S		
_____ SA		
_____ N		
_____ NA		
_____ O		
_____ OUA		
_____ NP		
_____ NAR		
_____ X _____ PENDING	Gerald Goldberg	6/4/1999

Prior state law required that \$10 million of the revenues generated from the in-lieu bank tax be transferred to the Local Agency Reimbursement Fund. The law specified that these revenues were to be distributed to cities, cities and counties, and counties, based on population and the proportion of the bank and financial corporations' employees' wages. The law was applicable for income years ending in 1980 and 1981.

SPECIFIC FINDINGS

Existing federal law requires states to treat national and state banks equally and prohibits states from imposing discriminatory taxes on national banks. The four methods outlined in the "Program History" discussion above have been deleted from federal law, thereby allowing states to use any system of taxation that satisfies the basic criterion of non-discrimination.

The California Constitution provides that the tax on state and national banks must be according to or measured by their net income and is in-lieu of all other taxes and license fees upon banks or their shares, except real property taxes and vehicle registration and license fees. However, the Constitution also gives the Legislature the power to override these provisions and provide for other taxes. **Existing state law** specifies that banks and financial corporations are covered under the in-lieu provisions and are subject to specific other taxes, such as local utility taxes, state energy resource taxes, and the state emergency telephone users surcharge. **Under existing state law**, the bank tax rate usually consists of the general corporation tax rate (currently 8.84%) plus the in-lieu rate of 2%. However, in the event a bank or financial corporation is a Subchapter S corporation, that corporation would be subject to the 1.5% tax rate for S corporations and the 2% in-lieu rate.

Existing state law provides that all moneys and remittances received by the department under the Bank and Corporation Tax Law (B&CTL) must be deposited in the Bank and Corporation Tax Fund. Moneys in the Bank and Corporation Tax Fund, upon order of the Controller, may be drawn from the fund to make tax refunds or be transferred to the General Fund.

Under the Administration of Franchise and Income Tax Law (AFITL), **this bill** would:

- require that the revenues attributable to the in-lieu tax be deposited into the Fund, which would be created by this bill, for disbursement to each city, county and city, and county. The department would determine by the last day in November and April the amount of revenues, net any refunds made, attributable to the 2% in-lieu tax. The FTB would notify the Controller within an unspecified number of business days of the amounts to be distributed. The distribution would be allocated among cities, counties and cities, and counties in accordance with a formula prescribed by the Legislature.
- require the Controller to transfer to cities, counties and cities, and counties by the 15th day of December and May, the amounts specified by the FTB.

Under the B&CTL, **this bill** would specify that the bank tax would not be in-lieu of nondiscriminatory parcel taxes enacted by cities, counties, and special districts according to the constitutionally required two-thirds vote of the voters and applied to all property owners at a uniform rate.

Implementation Considerations

This bill would require that the FTB determine by the last business day in November and April the amount of revenues to be deposited into the fund. However, the bill does not specify a beginning or an ending date for the period of calculation. It would assist the department if the bill specified those dates, provided the FTB with a period of time to determine the correct amount of revenue, and then provided time to report that information to the Controller.

This bill does not specify the commencing date when revenues would begin to be counted for purposes of determining the balance to be deposited into the Fund. The department could more easily implement the bill if it specified that the calculation of revenues would begin for returns filed after a certain date, since the filing of a return is the time that revenues are actually recorded by the department as received.

This bill specifies that the revenues, net of any refunds made, attributable to the 2% in-lieu rate would be transferred to the Fund. Since "revenues" are not specified, it is unclear whether the author intends that all tax, penalties and interest attributable to the 2% in-lieu rate be included in calculating amounts to go to the Fund. With some system changes, the department would be able to calculate the amount of tax attributable to the additional 2% in-lieu rate. However, if the author intends revenues to include penalties and interest, the department would have difficulty in determining the amounts properly attributable to the in-lieu rate since such a calculation could require the tracking and balancing of interest and penalties across a period of several years. This could result in significant additional costs for system programming, as well as requiring additional personnel time to determine the proper amount of revenue to be transferred.

This bill does not specify whether, in the event that the amount of tax paid is less than the amount owed, amounts attributable to the in-lieu rate would be calculated prior to or after the amounts attributable to the general tax rate, or to amounts attributable to the alternative minimum tax. Currently, taxes paid are applied to the minimum tax, general tax and then to the in-lieu tax rate. Additionally, the bill currently would provide that revenues would be transferred. Without further clarification as to the author's intent, the amount transferred would be limited to amounts actually collected, not those amounts owed.

TECHNICAL CONSIDERATION

The bill specifies that the revenues "attributable to the additional 2 percent tax rate specified in Section 23186" would be transferred. However, the additional rate prescribed in Section 23186 has varied over time and reference to the current rate of tax is not needed. A better approach would be to remove the reference to the 2% rate. Amendment 1 would resolve this issue.

FISCAL IMPACT

Departmental Costs

This bill provides that the department would be reimbursed for its costs from the Fund. If the implementation concerns identified above are resolved, costs would be less significant but could still be substantial due to the implementation of processes to separately calculate the in-lieu rate and the general tax rate. The department will be able to better estimate costs once the implementation concerns identified in this analysis are resolved.

Tax Revenue Estimate

Revenue losses to the General Fund under the B&CTL are estimated to be:

Effective With Fiscal Years Beginning 2000-01 (In Millions)		
2000-01	2001-02	2002-03
-\$139	-\$147	-\$156

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this measure.

Tax Revenue Discussion

Revenue losses to the General Fund under the B&CTL will depend on the amount of profits reported by banks and other corporations subject to the in-lieu tax rate.

The above estimate was based on the actual revenue collected from the in-lieu rate for the 1996 tax year (\$120 million) and projected to 2000-01 using the Department of Finance projected growth in corporate revenues.

BOARD POSITION

Pending.

Analyst	Colin Stevens
Telephone #	845-3036
Attorney	Patrick Kusiak

FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO AB 24
As Amended April 15, 1999

AMENDMENT 1

On page 4, line 30, strike: "2 percent tax"