Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author: Cardenas | Analyst: Colin Stevens | Bill Number: AB 83

Related Bills: AB 701, AB 2065 (1997-1998) | Telephone: 845-3036 | Introduced Date: 12/9/98

Attorney: Doug Bramhall | Sponsor:

SUBJECT: Local Business License, Permit, Taxes & Registration Fees/Prohibit Imposing On Persons Who Work From Residence

SUMMARY

Under the Business and Professions Code, this bill would prohibit a city, county, or city and county from requiring that a person who does not meet certain activity thresholds obtain a business license or permit or pay a business tax or registration fee solely because that person receives income reportable on federal From 1099-MISC for work performed at home.

EFFECTIVE DATE

This bill would take effect January 1, 2000.

SPECIFIC FINDINGS

Under federal law, with limited exceptions, every person, corporate or otherwise, engaged in a trade or business who, in the course of that business, makes payments aggregating $600 or more to another person (e.g. an independent contractor) in a calendar year must file an information return (Form 1099-MISC) with the name and address of the payee and the amount paid. Reportable payments include but are not limited to rent, salaries, wages and compensations.

Under **current state law,** a city or city and county may levy a regulatory license, business license fee or tax. Local business license taxes frequently are based on a business' gross receipts. Some cities have local ordinances that require an individual working from home to obtain a business license and pay the associated license fees and taxes. In some cities, zoning ordinances determine what type of business is an acceptable home occupation.

Current state law requires that each city that maintains a computerized record-keeping system or has access to such a system and that assesses a business license tax or fee furnish annually to the Franchise Tax Board (FTB) a list of all businesses subject to tax in the preceding year. This list must include:

- business name,
- address,
- federal employer identification number,
- type of business activity,
- amount of annual business tax, and
- any other information as the FTB may require.

Board Position:

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Department Director: **Gerald Goldberg** Date: **2-9-99**

When requested, the state reimburses cities for costs incurred in connection with furnishing this required information. **Currently,** the FTB uses information provided by cities and counties, the Board of Equalization (BOE) and the Department of Consumer Affairs occupational license program to identify taxpayers who have a license to operate a business but who have not filed a tax return for a given year. Once identified, the taxpayer is contacted by the FTB and requested to either file a return or notify the department why a return was not filed. If a taxpayer does not comply with the request for information or fails to file a required tax return upon notice and demand, the FTB may issue a proposed assessment based on available information.

Under the Business and Professions Code, this bill would prohibit a city, county, or city and county from imposing a business tax or registration fee, or from requiring that a person obtain a business license or permit solely because that person works at home and has received income required to be reported on Internal Revenue Service Form 1099-MISC, provided that person:

- Has not filed a fictitious business name statement; or
- Does not regularly solicit business at the person's place of business by advertisement.

Implementation Considerations

By eliminating the requirement that certain segments of self-employed taxpayers obtain business licenses, this bill would reduce by a small amount the number of taxpayers whose information FTB receives from local governments through the filing enforcement program. However, since FTB also receives reports from the Board of Equalization and Department of Consumer Affairs, FTB should be able to identify some of the taxpayers operating home-based businesses from other sources.

This bill defines "regularly" as at least one time in a three-moth period. This definition is somewhat ambiguous since, depending on the three-month period examined, one advertisement can meet the "regular" threshold. A definition of at least four times in any calendar year might more accurately reflect regular advertising.

FISCAL IMPACT

Departmental Costs

This bill is not expected to significantly impact the department's costs.

Tax Revenue Estimate

Based on data and assumptions discussed below, this bill would result in the following revenue losses.

Estimated Revenue Impact of AB 83 As Introduced 12/9/98 [$ In Millions]		
1999-00	2000-01	2001-02
minor loss	minor loss	minor loss

A minor loss is on the order of $250,000. The bill would be effective with income years beginning on or after January 1, 1999, with enactment assumed after June 30.

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

The revenue impact of this bill would be determined by the net of: (1) revenue losses attributed to fewer assessments and potentially less compliance on a self-assessed basis by taxpayers performing work at or from home under specified conditions and (2) revenue gains attributed to lower business expense deductions (city or county license fees no longer incurred or deducted) on self-assessed returns. The revenue impact of each component would be determined by the number of taxpayers who receive income for work performed at or from home under specified conditions, any unreported business income, reduced business deductions, and marginal tax rates of these taxpayers.

Each year the department receives in excess of one million business records from city business license sources for individuals that own businesses. Income tax assessments (issued through the PIT filing enforcement program) that are based on city business license sources average about $12 million in collections annually. It is not known how much of that $12 million is related specifically to taxpayers with home-based business activity, although, it is believed to be between 20% and 40%. For the estimate, one-quarter of the $12 million (or $3 million) is assumed attributable to home-based businesses. If half of the $3 million were attributed to business activities specified in the bill, and if half of that amount would not have been identified through other information sources, revenue losses would be on the order of $750,000. Once taxpayers and/or unreported sources of income are identified and assessed, compliance on a self-assessed basis by these taxpayers improves in subsequent taxable years.

Revenue gains due to fewer city or county business license fees being deducted as business expenses would probably not exceed $500,000 (assumes an average annual fee of $100 and a marginal tax rate of 5% for 100,000 taxable home businesses). On balance, net revenue losses would be on the order of $250,000.

BOARD POSITION

Pending.