Franchise Tax Board

ANALYSIS OF AMENDED BILL

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Related Bills:	See Legislative History	Telephone:	845-3410	Amended Date:	03/09/2000
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Exclusion/Interest Received From Smog Impact Fee Refunds

SUMMARY OF BILL

Under the Personal Income Tax Law (PITL), this bill would exclude from the gross income of taxpayers who were not allowed to deduct the vehicle smog impact fee any interest paid by the state in conjunction with the refund of the smog impact fee.

Under the Vehicle Code, this bill would establish a procedure for refunding the smog impact fee. These changes do not affect the department and are not discussed in this analysis.

SUMMARY OF AMENDMENT

The March 9, 2000, amendments made various changes to the Vehicle Code provisions, which do not affect the department.

The February 29, 2000, amendments modified and renumbered the PITL provisions regarding the gross income exclusion, as discussed in this analysis.

The February 24, 2000, amendments added PITL provisions regarding the gross income exclusion.

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

EFFECTIVE DATE

As an urgency statute, this bill would become effective immediately upon enactment and would apply to taxable years beginning on or after January 1, 2000.

LEGISLATIVE HISTORY

SB 215 (2000) would repeal the smog impact fee and appropriate $665 million from the General Fund to the Smog Impact Fee Refund Account to make the refunds as provided in this bill. This bill and SB 215 are linked, and each must be enacted for the other to be effective and for the entire refund program to be enacted.

AB 1109 (Stats. 1990, Ch. 453) imposed a vehicle smog impact fee of $300 on a person applying to register a vehicle that previously was registered outside California.

Board Position:			Department Director	Date
____ S	____ NA	____ NP		
____ SA	____ O	____ NAR	Alan Hunter for GHG	3/27/00
____ N	____ OUA	_X_ PENDING		

PROGRAM HISTORY/BACKGROUND

In October 1999, the 3rd District Court of Appeal ruled unconstitutional the $300 smog impact fee imposed on vehicles brought into California from other states. The smog impact fee was collected on about 1.7 million vehicles during the nine years it was in effect.

SPECIFIC FINDINGS

Existing federal and state laws provide that gross income includes all income from whatever source derived, including compensation, business income, gains from property, dividends, rents, interest, and royalties, unless it is specifically exempt.

Existing federal and state laws provide that certain types of income are excluded from the general gross income, such as amounts received from certain death benefits, gifts and inheritances, compensation for injuries and sickness, qualified scholarships, educational assistance programs, and foster care payments.

Under existing federal and state laws, a taxpayer, whether a corporation, individual, partnership, or an estate or trust, generally may deduct from gross income the ordinary and necessary expenses of carrying on a trade or business. Under this rule, the smog impact fee was deductible as a trade or business expense to the extent it was incurred by the taxpayer in carrying on the taxpayer's trade or business. For these taxpayers, the refund of the smog impact fee and the interest thereon would be included as income.

For taxpayers who file under the PITL and itemize their deductions, the property tax portion of the vehicle registration fee may be deducted. However, because the smog impact fee was not a tax, it was not deductible. Therefore, the refund of the smog impact fee for these taxpayers, along with taxpayers who took the standard deduction, would not be included as income; however, without this bill, the interest thereon would be included as income.

This bill would exclude from the gross income, for state tax purposes but not federal, for only those PIT taxpayers who were not allowed to deduct the vehicle smog impact fee any interest paid by the state in conjunction with the refund of the smog impact fee.

Policy Considerations

This bill would create differences between federal and California tax law, thereby increasing the complexity of California tax return preparation.

Implementation Considerations

Implementing this bill would occur during the department's normal annual update.

Technical Considerations

Amendment 1 would clarify that the word "deduct" means an income tax deduction.

FISCAL IMPACT

Departmental Costs

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

Tax Revenue Estimate

Based on the data and assumptions below, revenue losses are estimated as follows:

Revenue Impact of AB 809 Fiscal Year Impact (In Millions)		
2000-01	2001-02	2002-03
-$4	-$1	Minor Loss

- Minor Loss = Less than $500,000

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

Revenue Discussion

The revenue impact of this bill would depend upon the number of individuals receiving the smog impact fee refund, the amount of interest received pertaining to the refund that is excluded from gross income under the provisions of this bill, and the average marginal tax rate of qualified taxpayers.

According to the Department of Motor Vehicles (DMV) approximately 1.7 million vehicle owners were assessed smog impact fees. Of this total, DMV estimates that approximately 1.4 million will be issued refunds totaling approximately $546.3 million ($431 million for the smog fee and $115.3 million in calculated interest). This estimate assumes that 85% of vehicle owners will either file for the refund or that DMV will be able to locate vehicle owners through record searches. As of March of 2000, DMV has received approximately 250,000 claims for the smog impact fee refund. DMV estimates that approximately 75% of the refunds will be processed and refunded to taxpayers in taxable year 2000, 15% in 2001, and 10% in 2002.

Additionally, it was assumed that approximately 95% of interest payments received would qualify for the exclusion from gross income. Assuming an average marginal tax rate of 4.6% (based on the department's personal income tax model which allows for non-taxable filers) and the average interest payment per claim of $80, the first year revenue loss is estimated to be $4 million (75% x 1.4 million in total claims X $80 interest payment X 4.6% average marginal tax rate X 95% = $4 million).

BOARD POSITION

Pending.

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FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO AB 809
As Amended March 9, 2000

AMENDMENT 1

On page 4, modify lines 20 and 21, as follows:

17139.5. For taxpayers who were not allowed ~~to deduct~~ a deduction under Article 6 (commencing with Section 17201) of Chapter 3, for the vehicle smog impact fee imposed by Section