

SUMMARY ANALYSIS OF AMENDED BILL

Author: Eduardo Garcia & Medina Analyst: Diane Deatherage Bill Number: AB 185
 Related Bills: See Prior Analysis Telephone: 845-4783 Amended Date: May 20, 2015
 Attorney: Bruce Langston Sponsor _____

SUBJECT:	California New Markets Tax Credit
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SUMMARY

This bill would allow a credit, under the Personal Income Tax Law (PITL) and Corporation Tax Law (CTL), in modified conformity with the federal New Markets Tax Credit.

This analysis only addresses the provisions of this bill that impact the department’s programs and operations.

RECOMMENDATION

No position.

SUMMARY OF AMENDMENTS

The May 20, 2015, amendments made nonsubstantive technical changes and resolved all of the technical considerations. Except for the “This Bill” and “Technical Considerations” sections, the remainder of the department’s analysis of the bill as introduced January 25, 2015, still applies. The “Economic Impact” and “Fiscal Impact” sections and outstanding concerns have been restated below for convenience.

THIS BILL

For taxable years beginning on or after January 1, 2016, and before January 1, 2028, this bill would, under both the PITL and CTL, allow a cumulative credit, as described below, equal to 39 percent of a taxpayer’s qualified equity investment. The credit would be repealed by its own terms as of December 1, 2028.

The credit would mirror the federal New Markets Tax Credit provisions, with the following modifications:

- Authorize the California Governor’s Office of Business and Economic Development (GO-Biz) and the California Competes Tax Credit Committee (Tax Credit Committee) to administer the California New Markets Tax Credit Program.
- Replace references to "Secretary" with "GO-Biz," for allocation of the limitation.
- Allow a 39 percent credit to be claimed in the following manner:
 - Zero percent for the first two credit allowance dates;
 - Seven percent on the third credit allowance date; and
 - Eight percent on each of the remaining credit allowance dates (fourth through seventh).

Board Position:	Legislative Director	Date
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- Allow the credit to a taxpayer that holds the qualified equity investment on the credit allowance date and the six subsequent anniversaries of the credit allowance date.
- Require that a CA Development Entity, be an entity that has an allocation agreement dated on or after January 2, 2012, with the Community Development Financial Institutions Fund of the U.S. Treasury that includes California within the service area.
- Require the qualified low-income community to be in California.
- Limit eligibility as a "qualified active low-income community business" to businesses located within census tracts that meet one of the following:
 - Poverty rate is greater than 30 percent;
 - Median family income is equal to or less than 60 percent of the California median family income, if located within a non-metropolitan area;
 - Median family income is equal to or less than 60 percent of the greater of the California median family income or metropolitan area median family income, if located within a metropolitan area; or
 - Unemployment rate is at least 1.5 times the national average.
- Allow startup businesses to be considered a qualified active low-income community business for California purposes.
- Provide that a qualified active low-income community business would include an operating business that, at the time the initial investment is made, has 250 or less employees and is located in a low-income community.
- Provide that certain types of businesses would be excluded from qualifying as a qualified active low-income community business (i.e., country club, gaming establishment, massage parlor, liquor store, golf course, charter school, or a sexually oriented business).
- Provide that GO-Biz would recapture the credit claimed on a return when:
 - Any portion of the federal New Markets Tax Credit has been recaptured. In this case, GO-Biz's recapture would be proportionate to the federal recapture with respect to the qualified equity investment.
 - The CA Development Entity redeems a qualified equity investment prior to the seventh anniversary of the issuance of the qualified equity investment. In this case, GO-Biz's recapture would be proportionate to the amount of the redemption with respect to the qualified equity investment.
 - The CA Development Entity fails to (1) invest at least 85 percent of the purchase price of the qualified equity investment in qualified low-income community investments in California within 12 months and (2) maintain at least 85 percent of such level of investment in qualified low-income community investments in California until the last credit allowance date.
- Allow credits in excess of a taxpayer's current year tax liability to be carried forward for seven subsequent years.

- Allow an aggregate annual amount of allocation of authority to designate qualified equity investments for each calendar year based upon credits of up to \$40 million, in addition to any undesignated or reissued allocations of authority to designate qualified equity investment from the prior year. The maximum amount of allocation of authority to designate qualified equity investments allocated over the life of this program would result in an amount based on an aggregate credit cap of \$200 million.
- This bill would require the California Alternative Energy and Advanced Transportation Financing Authority to annually determine the difference between the \$100 million statutory limitation on the sales and use tax exclusion and the amount assigned during the calendar year. The difference would be made available to the Tax Credit Committee for award of authority to designate qualified investments to CA Development Entities in the following calendar year under the California New Markets Tax Credit Program.

This bill would require GO-Biz to accept applications on or before May 15, 2016, and award authority to designate qualified equity investment annually through 2020.

GO-Biz would be required to establish and impose reasonable fees upon entities that apply for the authority to designate qualified equity investments and develop guidelines to adopt an allocation process that would do the following:

- Create an equitable distribution process for allocation of the authority to designate qualified equity investments;
- Set minimum organizational capacity standards;
- Require annual reporting to GO-Biz by each CA Development Entity that receives an allocation; and
- Provide that any allocation of undesignated qualified equity investments is returned to GO-Biz for subsequent reallocation.

GO-Biz would develop guidelines for its responsibilities with respect to the allocation of the qualified equity investments and recapture of credit.

This bill would provide that the guidelines would not be subject to the rulemaking requirements of the Administrative Procedure Act.

A CA Development Entity would provide GO-Biz with the name, address, and tax identification number of each investor and entity for which an authority to designate qualified equity investments was allocated by the CA Development Entity. The Tax Credit committee would provide this information to the Franchise Tax Board (FTB) in a manner determined by the FTB.

GO-Biz would be required to post the information, on its Web site, from the annual reporting by the CA Development Entities and the geographic distribution of the qualified active low-income community businesses assisted.

This bill would create the California New Markets Tax Credit Fund for the fees imposed on CA Development Entities that apply for the allocation of the authority to designate qualified equity investments. GO-Biz and the Tax Credit committee would only make awards in a calendar year in which the Legislature appropriates funds from the California New Markets Tax Credit Fund.

The cap for the credit provided by this bill would be based on previously authorized expenditures from the California State Sales and Use Tax Exclusion Program.¹

This bill would add severability language that would, upon a provision or application of a provision being invalidated by a court, allow the remaining provisions to remain in effect.

FISCAL IMPACT

This bill would impact the department's printing, processing, and programming costs. As the bill continues to move through the legislative process, costs will be identified and an appropriation will be requested, if necessary.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of AB 185 As Amended May 20, 2015 Assumed Enactment After June 30, 2015 (\$ in Millions)				
2015-16	2016-17	2017-18	2018-19	2019-20
\$0.0	\$0.0	-\$1.8	-\$5.8	-\$11.0

This analysis does not account for changes in employment, personal income, or gross state product that could result from this bill. In addition, this estimate only reflects the revenue impact to income and franchise taxes.

Revenue Discussion

This bill would establish the California New Markets Tax Credit Program for investments in businesses that provide capital or loans to low-income communities. This estimate assumes that the \$40 million annual maximum credit would be made each year from 2016 through 2020. It also assumes that \$26 million of the credit would be used to offset income and franchise taxes and the remainder would be used against insurance taxes.

¹ Revenue and Taxation Code section 6010.8.

As specified in this bill, taxpayers may not claim any credit in the first two years after making a qualified investment. In addition, the portion of the credit that may be claimed would be 7 percent in the third year and 8 percent in years four through seven. Based on these credit limitations and the annual allocation threshold, the 2016 investment allocation would generate \$4 million of credit in 2018 and approximately \$5 million annually in 2019 through 2022. The total cost over the life of the program would be capped at \$200 million.

Because taxpayers could not claim any credit the first two taxable years, there would be no revenue impact the first two fiscal years. Taxpayers may begin claiming the credit in the 2018 taxable year. Credit usage would be phased in beginning in 2018 and would peak in the 2022 taxable year with \$26 million and then begin to decline. The estimate is converted to fiscal years, rounded and reflected in the table above.

LEGAL IMPACT

Federal law allows states to impose a non-discriminatory franchise tax on federal securities. This bill would allow a credit for investment in entities that make loans to entities engaged in a trade or business in low-income communities. The credit would provide an indirect subsidy by encouraging these loans over investments in federal securities and more favorable tax benefits for making the loan instead of holding federal securities. As a result, this tax benefit could be considered to result in discrimination against investments in federal securities and thus a violation of the federal prohibition of discriminatory state taxation of federal securities.

SUPPORT/OPPOSITION²

Support: Advantage Capital Partners; California Association for Local Economic Development; California Association for Micro Enterprise Opportunity; California Bankers Association; California Communities United Institute; California Urban Partnership; Capital Impact Partners; City of Indian Wells; City of Lakewood; City of Thousand Oaks; Enhanced Capital; Enhanced Capital Partners; Fresno Community Development Financial Institution; Fresno Economic Opportunities Commission; Genesis LA Economic Growth Corporation; League of California Cities; Los Angeles County Economic Development Corporation; Northern California Community Loan Fund; Opportunity Fund; Orange County Business Council; Regional Economic Association Leaders of California; Small Business California; TELACU.

Opposition: The California Tax Reform Association.

² From Assembly Revenue and Taxation Committee analysis, dated May 15, 2015.

POLICY CONCERNS

This bill would allow a taxpayer to obtain combined federal and state credits equal to 74 percent of the investment even in cases where the federal credit alone would make the CA Development Entity's low-income community investment economically feasible. Consequently, the author may wish to provide that a specified degree of economic necessity is present before the CA Development Entity may market the state credit.

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