Franchise Tax Board

ANALYSIS OF AMENDED BILL

Author:	Campos	Analyst:	Davi Milam	Bill Number:	AB 1229
Related Bills:	See Legislative History	Telephone:	845-2551	Amended Date:	April 9, 2015
		Attorney:	Bruce Langston	Sponsor	

SUBJECT:	Rent Control Credit / Senior Citizen Rent Increase Exemption Program

SUMMARY

This bill would, under the Civil Code (CIV), establish the Senior Citizen Rent Increase Exemption (SCRIE) Program, and under the Personal Income Tax Law (PITL), create a tax credit for taxpayers whose tenants participate in the SCRIE Program.

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

RECOMMENDATION

No position.

Summary of Amendments

The April 9, 2015, amendments eliminated the bill's prior language related to property tax law and added the provisions discussed in this analysis. This is the department's first analysis of this bill.

REASON FOR THE BILL

The reason for this bill is to explore the economic and social impact of the SCRIE Program as a means to provide affordable housing to low-income seniors.

EFFECTIVE/OPERATIVE DATE

This bill would be effective January 1, 2016, and specifically operative for taxable years beginning on or after January 1, 2016, and before January 1, 2020.

FEDERAL/STATE LAW

Under federal and state law, gross income includes the money taxpayers receive for the occupancy of real estate. In general, all ordinary and necessary business expenses paid or incurred during the tax year in maintaining the rental property are deductible, subject to certain limitations.

Board Position:			Executive Officer	Date
______ S	______ NA	X NP	Selvi Stanislaus	4/29/15
______ SA	______ O	______ NAR		
______ N	______ OUA	______		

In general, rental activities by an individual, estate, trust, closely held C Corporation, or a personal service corporation are considered passive activities, and losses from passive activities may only be deducted up to the amount of income from passive activities. Any excess passive activity loss may be carried forward to future years.[1] Taxpayers who actively participate in their rental real estate activity and who meet certain adjusted gross income limitations may be able to deduct up to $25,000 of loss against nonpassive income.

Certain business related tax credits are limited to the tax attributable to the taxpayer's passive activities.

There are currently no federal or state credits comparable to the credit this bill would create.

THIS BILL

Under the PITL, for each taxable year beginning on or after January 1, 2016, and before January 1, 2020, this bill would allow a tax credit in an amount equal to the amount of rent not received for that taxable year by a taxpayer, who is a landlord, as a consequence of a tenant receiving a rent increase exemption order under the SCRIE Program (described below).[2]

This bill would allow any unused credit to be carried over eight years until exhausted.

This credit would remain in effect only until December 1, 2020, and as of that date would be repealed.

Under the CIV, this bill would establish the SCRIE Program, a demonstration project to be implemented in the County of Alameda, City and County of San Francisco, the County of Ventura, and the Country of Santa Clara. The SCRIE Program would allow an eligible head of household in a rent-controlled property to apply for an exemption from rent increases and to provide his or her landlord a tax credit in an amount equivalent to the rent increase that the landlord otherwise would have received if not for the exemption.

An eligible head of household renting a qualifying residence could apply to a supervising agency for a rent increase exemption order pursuant to the SCRIE program on and after April 1, 2016, and before the SCRIE Program's January 1, 2019, repeal date.

The supervising agency would be required to do all of the following:

- Review the application and confirm that the applicant is an eligible head of household and the property is a qualifying residence.
- Issue to the applicant a rent increase exemption order, which would be in effect for a 12-month period commencing the month following its issuance.

---

[1] In the year of disposition, any remaining suspended loss and the current year loss may be deducted.
[2] Established pursuant to Civil Code section 1954.532.

- Provide a copy of the order to the landlord and notify the landlord of the right to make a claim for a tax credit under R&TC section 17053 for rent not received pursuant to the order.

This bill also would require the eligible head of household to reapply and qualify for any subsequent order. A rent increase exemption order validly issued before the repeal of this provision would remain effective for its full 12-month term. The provisions of the bill establishing the SCRIE program would be effective until January 1, 2019, and repealed as of that date.

This bill would, under the CIV, define a number of terms and phrases including “rent increase exemption order.”

IMPLEMENTATION CONSIDERATIONS

The department has identified the following implementation concerns. Department staff is available to work with the author’s office to resolve these and other concerns that may be identified.

It is unclear how the department would verify the “amount of rent not received.” Lack of clarity could result in disputes between taxpayers and the department and would complicate the administration of this credit. The author may wish to amend this bill for clarity, for example, could the “amount of rent not received” be included on the exemption order?

The department would be unable to verify eligibility for the credit at the time a return is filed because the bill fails to require that a copy of the exemption order be provided to the FTB, by either the supervising agency or the taxpayer. To reduce taxpayer burden and for ease of administration, it is recommended that this bill be amended to require SCRIE Program exemption orders be provided to the department upon issue by the supervising agency.

LEGISLATIVE HISTORY

AB 697 (Chu, 2015/2016), would create a new renters’ credit for low-income seniors in certain counties. AB 697 is pending before the Assembly Revenue and Taxation Committee.

PROGRAM BACKGROUND

The California Department of Consumer Affairs reports that the following California cities have rent control ordinances: Berkeley, Beverly Hills, Campbell, East Palo Alto, Fremont, Hayward, Los Angeles, Los Gatos, Oakland, Palm Springs, San Francisco, San Jose, Santa Monica, Thousand Oaks, and West Hollywood.

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, and the other states surveyed lack an income tax credit for landlords comparable to the credit allowed by this bill; however, *Michigan* and *Minnesota* allow an income tax credit, based on property taxes, to both owners and renters, including those that are senior citizens.

Additionally, *Massachusetts* allows property tax abatement, up to $500, for senior-citizen owned property. *New York* also allows property tax abatement for certain rent-controlled property occupied by low-income seniors or disabled individuals. The abatement amount is based on the maximum allowable rent increase foregone by the landlord, and is certified by the local rent control agency.

FISCAL IMPACT

The department's costs to implement this bill have yet to be determined. As the bill moves through the legislative process and the implementation concerns are resolved, 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 AB1229 As Amended April 9, 2015 Assumed Enactment After June 30, 2015 ($ in Millions)		
2015-16	2016-17	2017-18
- $6.2	- $24	- $50

This analysis does not account for changes in employment, personal income, or gross state product that could result from this bill.

Revenue Discussion

According to the 2013 U.S. Census and 2012 Franchise Tax Board data, there are approximately 725,000 individuals, age 62 and over, living in Alameda, San Francisco, Santa Clara, and Ventura counties. Using various published sources, it is estimated that 45 percent of these individuals rent their homes. It is further estimated that 10 percent of these individuals live in rent controlled or rent stabilized housing and would meet the income qualifications required to apply for the rent exemption qualifying their landlord for the credit. This population is grown by the Department of Finance growth rate and results in an estimated 36,000 possible qualified applicants. It was assumed that 50 percent would apply for the rent exemption qualifying their landlord for the credit in year one, 70 percent in year two, and continue to increase each year the credit is available. This results in estimated applications filed of 18,000, 25,000, 30,000, and 34,000 for the years 2016 through 2019, respectively.

It is estimated that the average annual rent paid for rent controlled or rent stabilized housing would be $1,450 per month. Various housing board websites indicated that the average annual rent increase is 4 percent per year. Should the qualified individual apply each year, the amount of rent not received by the landlord would increase an additional 4 percent each additional year that the qualified individual applies for the credit. It is estimated that the average annual amount of rent not received would be $750 in year one, $1,500 in year two, and grow by $750 per year for each year thereafter. This results in an estimated credit generation of $13 million, $38 million, $68 million, and $100 million for the years 2016 through 2019, respectively. It is assumed that 75 percent of the credit would be used in the year generated and the remainder would be used over the next several years.

Landlords ordered, under the SCRIE program, to forgo an annual rent increase would have reduced income in the amount of the credit generated resulting in an estimated additional revenue loss of $800,000, $2.3 million, $4.2 million, and $6.5 million for the years 2016 through 2019, respectively.

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

SUPPORT/OPPOSITION

Support: SEIU California and SEIU-United Long-term Care Workers Union.

Opposition: None provided.

ARGUMENTS

Proponents: Some may say that this bill would encourage landlords that rent to eligible low-income seniors to defer or forego rent increases, thus, improving the financial security of these economically fragile individuals.

Opponents: Some may argue that this bill is overly narrow and should be broadened to assist all low-income seniors living in rental housing in the state.

POLICY CONCERNS

This bill fails to limit the amount of the credit that may be taken. Generally, credits are limited as a percentage of amounts paid or incurred or on a per-taxpayer basis. This bill would allow 100 percent of the" amount of rent not received" as a credit, which is unprecedented.

This bill would provide a tax benefit for individuals and entities subject to tax under the PITL that would not be provided to other business entities such as corporations. Thus, this bill would provide differing treatment based solely on classification.

Certain business-related tax credits (e.g., low-income housing credit and research credit) are limited to the tax attributable to the taxpayer's passive activities. These credits are known as passive activity credits. The purpose of this limitation is to prevent taxpayers from using a credit from a passive activity to offset tax attributable to other income. Since this credit is not included in the list of passive activity credits, taxpayers who generate this credit from a passive activity would be able to use the credit to offset tax attributable to any income.

LEGISLATIVE STAFF CONTACT

Davi Milam
Legislative Analyst, FTB
(916) 845-2551
davi.milam@ftb.ca.gov

Jame Eiserman
Revenue Manager, FTB
(916) 845-7484
jame.eiserman@ftb.ca.gov

Gail Hall
Legislative Director, FTB
(916) 845-6333
gail.hall@ftb.ca.gov