

Legal Division Guidance 2011-01-01

(Impact of Proposition 26 on SB 401)

Question: How will the adoption of Proposition 26 impact FTB's enforcement of SB 401?

Answer:

Background

SB 401, enacted April 12, 2010, but effective January 1, 2011, and generally operative for taxable years beginning on or after January 1, 2010, conforms to numerous provisions of the Internal Revenue Code that were amended by various federal acts enacted by the federal government after January 1, 2005. Following the enactment of SB 401, Proposition 26, approved by the voters on November 2, 2010, amended section 3 of Article XIII A of the Constitution by:

- Amending the existing text of section 3 of Article XIII A to read:
"(a) Any change in state statute which results in any taxpayer paying a higher tax must be imposed by an act passed by not less than two-thirds of all members elected to each of the two houses of the Legislature [.]"
- Adding new subsection (c) to section 3 of Article XIII A that provides as follows:
“(c) Any tax adopted after January 1, 2010, but prior to the effective date of this act [November 3, 2010], that was not adopted in compliance with the requirements of this section is void 12 months after the effective date unless the tax is reenacted by the Legislature and signed into law by the Governor in compliance with the requirements of this section.”

Discussion

There is significant ambiguity regarding the scope and meaning of language above. For example, as a technical matter, while initiatives are adopted, statutes are 'enacted.' The use of the term 'void' raises questions about possible retroactive operative effect on any 'tax adopted' after January 1, 2010, if the subject legislation is not 'reenacted' by November 3, 2011. If a 'tax' is not reenacted, is the entire act void or is the tax-increasing provision severable from other aspects of the act?

SB 401 is the law – for now

There is no basis to believe that SB 401 is not valid law – at least for the 12 month period following the adoption of Proposition 26. As a result, it's our view that the Franchise Tax Board is required to and we are applying the provisions of SB 401 for periods for which it is applicable.

Constitution Requires FTB to Apply SB 401 Until Determination By An Appellate Court

There is considerable uncertainty regarding the continuing viability of the provisions of SB 401 if the Legislature fails to take any action prior to November 3, 2011, with respect to SB 401 or any of the provisions contained therein. However, after careful consideration of applicable law, it appears that the Constitution of California, in particular section 3.5 of Article III, requires FTB to enforce SB 401 even after the adoption of Proposition 26. Section 3.5 of Article III prohibits an administrative agency, such as FTB, from declaring a statute invalid or unenforceable in the absence of an appellate court determination that the statute is unenforceable or unconstitutional. As a result, FTB is required to enforce SB 401 until an appellate court has made a determination that some portion or all of SB 401 is 'void' pursuant to Proposition 26 and, therefore, unenforceable.