STATE OF CALIFORNIA
Franchise Tax Board

Analysis of Amended Bill

Author: Quirk-Silva, et al.	Sponsor:	Bill Number: AB 1765
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Subject: Disaster Loss Credit

Summary

This bill would, under the Personal Income Tax Law (PITL), create a tax credit for taxpayers that sustained uncompensated losses as a result of a disaster.

Recommendation – No position.

Summary of Amendments

The May 15, 2018, amendments removed provisions related to the Building Homes and Jobs Act and replaced them with the provisions discussed in this analysis.

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

Reason for the Bill

The reason for the bill is to assist those impacted by a disaster by offering a tax credit.

Effective/Operative Date

As a tax levy, this bill would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2019, and before January 1, 2020.

Federal/State Law

Under federal and state law, a disaster loss occurs when business or personal property is completely or partially destroyed as a result of a fire, storm, flood, or other natural event.

Internal Revenue Code (IRC) section 165(i), allows a taxpayer that suffers a disaster loss to elect to deduct the loss in the year immediately preceding the year the disaster occurred if it is a Presidentially-declared disaster loss.

California law conforms to IRC section 165(i) allowing taxpayers to elect to file an amended return to deduct a disaster loss in the taxable year prior to the loss year, for any Presidentially-declared disaster and for taxable years beginning on or after January 1, 2014, and before January 1, 2024, any disaster proclaimed by the Governor regardless of a Presidential declaration.[1]

Existing federal and state law allows an individual taxpayer with a disaster loss that is not reimbursed by insurance or otherwise, to deduct disaster losses to the extent that each loss exceeds $100 and aggregate net losses for the taxable year exceed 10 percent of adjusted gross income. Business and income-producing property are not subject to these limitations.

If a disaster loss deduction creates a net operating loss, the carry forward treatment and carryback treatment apply. However, for losses arising in taxable years after December 31, 2017, federal law does not allow carryback treatment.

This Bill

This bill would, under the PITL, for taxable years beginning on or after January 1, 2019, and before January 1, 2020, allow a tax credit in an amount equal to 50 percent of the amount paid or incurred by a taxpayer, not to exceed $1,000, for uncompensated losses sustained by a taxpayer and not compensated for by insurance or otherwise that occurred in a qualified disaster area as a result of the disaster that is the subject of the Governor's declaration.

"Qualified disaster area" means an area where the Governor declared a disaster between July 1, 2017, and January 31, 2018.

The bill would allow any excess credit to be carried over for up to six years, until exhausted.

The credit would be excluded from the requirements of Section 41.

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 whether the $1,000 limitation would apply to the credit or the expenses paid or incurred for the uncompensated loss by the taxpayer. To ensure clarity and consistency with the author's intent, it is recommended the bill be amended.

[1] Revenue & Taxation Code section 17207.14.

The bill provides a credit for “amounts paid or incurred as a result of a disaster for losses sustained”. However, taxpayers don't pay for “losses” under the tax laws; rather, it appears the bill's intent is to provide a credit for expenditures made (that are not compensated by insurance) by taxpayers in response to losses sustained by that taxpayer as a result of certain disasters that have occurred. If this is the author's intent, the bill should be amended.

Because the bill fails to specify otherwise, the credit would be available for uncompensated losses sustained by a taxpayer in the specified disaster zones. If it is the author’s intent to limit the credit to uncompensated disaster losses, the bill should be amended.

Legislative History

No similar legislation has been identified.

Other States’ Information

Florida, Massachusetts, Michigan, Minnesota, and *New York* laws do not provide a credit comparable to the one allowed by this bill. The laws of these states were selected due to their similarities to California's economy, business entity types, and tax laws.

Illinois provides a disaster loss credit equal to the lesser of $750 or the taxpayer’s casualty loss deduction allowed with respect to the qualified real property under IRC section 165.

Fiscal Impact

The department’s costs to implement this bill have yet to be determined. As the bill moves through the legislative process, costs will be identified.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of AB 1765 as Amended May 15, 2018
Assumed Enactment after June 30, 2018

($ in Millions)

Fiscal Year	Revenue
2018-2019	0
2019-2020	- $600
2020-2021	- $200

This analysis does not account for changes in employment, personal income, or gross state product that could result from this bill or for the net final payment method of accrual.

Revenue Discussion

This estimate calculates the impact of both uncompensated disaster losses and other losses sustained by taxpayers between July 1, 2017, and January 31, 2018, in areas declared to be disaster areas by the Governor during that period.

Utilizing data available from the Department of Insurance and data on casualty and theft losses from personal income tax returns, it is estimated that uncompensated losses impacted 126,000 taxpayers from July 2017 through January 2018. Because "loss" is undefined in the bill, the number of taxpayers with unreimbursed losses associated with insurance claims is increased by 40 percent or to 180,000 taxpayers to account for taxpayers who live in disaster areas that claim losses unrelated to disasters. In addition, for the same reason, it is assumed that losses unrelated to insurance claims would also be used in the calculation of the credit. Based on the Franchise Tax Board (FTB) tax data, approximately 8.5 million tax returns are filed by taxpayers living in the disaster areas declared by the Governor during the period specified. It is assumed that 10 percent, or 850,000 taxpayers, would incur other losses and be eligible for the credit. This estimate assumes taxpayers would claim the maximum credit of $1,000 resulting in total credits generated of approximately $1 billion in the 2019 taxable year.

Based upon the FTB tax data, it is estimated 80 percent of the taxpayers would have sufficient tax liability to claim the credit in the year generated. For those taxpayers, 75 percent or approximately $600 million of the credit would be used in the 2019 taxable year. The remaining credits would be utilized in the following year.

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

Support/Opposition

Support: None provided.

Opposition: None provided.

Arguments

Proponents: Some may argue that this bill would bring much needed financial relief to those impacted by a disaster during this timeframe.

Opponents: Some may argue that this bill is overly narrow by providing relief only to those impacted by a disaster loss during the limited timeframe specified.

Policy Concerns

This bill would allow taxpayers in certain circumstances multiple benefits for the same item of expense.

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