Summary Analysis of Amended Bill

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Related Bills: See Prior Analysis
Bill Number: AB 3072
Amended: May 16, 2018

Subject: Low-Income Housing Credit/Farmworker Housing Credit

Summary

This bill would, under the Personal Income Tax Law (PITL) and the Corporation Tax Law (CTL), modify the Low-Income Housing Credit (LIHC).

This bill would also modify provisions of the Insurance Tax Law. This analysis only addresses the provisions of the bill that impact the department’s programs and operations.

Recommendation – No position.

Summary of Amendments

The May 16, 2018, amendments modified the operative dates for increasing the amounts available for allocation by the California Tax Credit Allocation Committee (Allocation Committee), and for the elimination of the limitation on the use of the LIHC credit relating to the passive activity loss rules; modified the amount available for allocation by the Allocation Committee for farmworker housing; and modified certain application requirements.

The May 16, 2018, amendments resolved the policy concern discussed in the department’s analysis of the bill as amended on March 22, 2018, and April 17, 2018, and an additional technical consideration was identified.

Except for the “Effective/Operative Date,” “This Bill,” “Technical Considerations,” “Economic Impact,” and “Policy Concerns” sections, the remainder of the department’s analysis of the bill as amended on March 22, 2018, and April 17, 2018, still applies. The “Implementation Considerations” and “Fiscal Impact” sections have been updated and restated below for convenience.

Effective/Operative Date

As a tax levy, this bill would be effective immediately upon enactment. The provisions affecting the computation of tax due to changes in passive activity losses and credits would be specifically operative for taxable years beginning on and after January 1, 2018, and before January 1, 2024.
The provisions increasing amounts available for allocation by the Allocation Committee would be specifically operative for allocations made during or after calendar year 2019 and through the 2023 calendar year, inclusive, except that the provision decreasing the allocations to farmworker housing would be specifically operative beginning with the 2024 calendar year.

The provisions modifying definitions and the LIHC’s applicable percentage would be specifically operative as of January 1, 2018.

This Bill

This bill would, for purposes of the LIHC, modify the definitions of:

- “Taxpayer” to include members of a limited liability company (LLC).
- “Housing sponsor” to include LLCs.
- “Extremely low income households” and “Very low income households” to have the same meanings as in Section 50053 of the Health and Safety Code.

This bill would recast the LIHC applicable percentages as follows:

- For a new building that is not federally subsidized, the applicable percentage for years 1 through 3 would be the amount determined pursuant to Internal Revenue Code section 42(b)(1) and for year 4 would be the difference between 30 percent and the sum of the applicable percentages for years 1 through 3.
- For a new building that is federally subsidized, 15 percent for the first three years and 5 percent for the fourth year.
- For an existing building that is federally subsidized, the applicable percentage for years 1 through 3 would be the amount prescribed by the Secretary of the Treasury for new buildings that are federally subsidized for the taxable year, and for year 4 would be the difference between 13 percent and the sum of the applicable percentages for years 1 through 3.
- For any qualified low-income building that meets all of the following criteria, the applicable percentage would mean 30 percent for each of the first three years and 5 percent for the fourth year. Additionally, a qualified low-income building that received this increased allocation would be ineligible for an allocation under the prior bulleted item.
  - Is at least 15 years old.
  - Is serving households of very low income or extremely low income whose maximum household income is not more than 45 percent of the area median gross income, as specified.
  - Would have insufficient credits under the second and third bulleted items above to complete substantial rehabilitation due to a low appraised value.
  - Will complete the substantial rehabilitation in connection with this increased credit allocation regime.
Beginning for allocations made by the Allocation Committee during calendar year 2019, and for the 2020 through 2023 calendar years, inclusive, this bill would:

- Increase the LIHC allocation amount by an additional $300 million, and for the 2020-2023 calendar years, subject the allocation to indexing for inflation as specified.
- Increase the annual amount available for allocation to farmworker housing projects from $500,000 to $25 million. For the 2024 calendar year and thereafter, the amount would return to $500,000. Unallocated amounts for a calendar year would be added to the total LIHC allocation amount available for the following calendar year.

Because this bill would be effective and operative immediately upon enactment, this bill would for the taxable year 2018, conform to the federal passive activity loss limitation applicable to rental real estate relating to low-income housing of $25,000.

For taxable years beginning on or after January 1, 2019, and before January 1, 2024, this bill would, under the PITL and CTL, eliminate the passive activity loss limitation applicable to rental real estate relating to low-income housing. For taxable years beginning on or after January 1, 2024, this bill would reinstate a $75,000 limitation.

This bill would, under the PITL only, for LIHC allocations made on or after January 1, 2019, require that a housing sponsor subject to the PITL demonstrate that it will invest an amount in the project at least equal to the amount of credit allocated to it.

**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.

Unlike the PITL provisions, the CTL provisions lack the requirement that a housing sponsor demonstrate that it will invest an amount in the project at least equal to the amount of credit allocated in order to receive an allocation on or after January 1, 2019. If this is contrary to the author’s intent, this bill should be amended.

Additionally, it is unclear whether taxpayers subject to the CTL who are partners in a partnership or LLC that is allocated the credit by the Allocation Committee, would be subject to the investment limitation on their distributive share of the LIHC that flows through to them from the partnership or LLC.

**Technical Considerations**

The May 16, 2018, amendments lack language specifying the passive activity loss limitation applicable to rental real estate relating to low-income housing applicable to taxable year 2018, thus conforming to the federal limitation of $25,000 for that year. To reinstate the state limitation of $75,000 for taxable year 2018, subdivision (d) of Section 17561 and subdivision (e) of Section 24692 need to be amended.
The references to LLC in the PITL and CTL are unnecessary. The following four amendments are recommended:

On page 17, line 33, strike “members in the case of a limited liability company”

On page 17, lines 37-38, after “partnership” strike “the limited liability company in the case of a limited liability company”

On page 34, line 9, after “partnership,” strike “members in the case of a limited liability company”

On page 34, lines 13-14, after “partnership,” strike “the limited liability company in the case of a limited liability company”

**Fiscal Impact**

The department’s costs to implement the provisions of 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 impact:

Estimated Revenue Impact of AB 3072 as Amended May 16, 2018
Assumed Enactment after June 30, 2018

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018-2019</td>
<td>- $5.2</td>
</tr>
<tr>
<td>2019-2020</td>
<td>- $22.0</td>
</tr>
<tr>
<td>2020-2021</td>
<td>- $44.0</td>
</tr>
</tbody>
</table>

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. In addition, this estimate only reflects the revenue impact to income and franchise taxes.

**Revenue Discussion**

Using LIHC allocation data from the Allocation Committee, it is assumed that the maximum credit allocation threshold would be reached each year. This bill authorizes an additional $300 million in LIHC allocations beginning for allocations made during calendar year 2019 through calendar year 2023. It is assumed that five percent, or $15 million, of the allocation would ultimately be returned to the Allocation Committee due to unforeseen project issues. According to Farmworker Housing allocation data from the Allocation Committee, $3.4 million
in farmworker state tax credits were awarded in 2017, leaving $2.7 million awaiting allocation in 2018. Because prior allocations of the Farmworker housing credit were infrequent, the $25 million credit allocation is modeled as a one year allocation lag, this lag is applied to each year. For example, the $25 million would be set aside in tax year 2019, and then added back in tax year 2020. This set aside is only applied through calendar year 2023, when it returns to $500,000 reserve per calendar year.

Based on total current LIHC awards and usage, it is estimated that 75 percent, or $195 million, of the annual credits would be used to offset income and franchise taxes and the remainder would be used against insurance taxes, which is not included in the above table. Based on current LIHC usage, it is assumed that 70 percent, or $135 million, of the credit would be used over the four year credit period and the remaining 30 percent would be carried forward to future years. It is further assumed that 25 percent of the carry forward would be sold at 80 percent of its face value causing the seller to recognize capital gains in the year of the sale. It is assumed these amounts would be used over the four year credit period.

Allocated credits cannot be used until after the building has been put into service. As a result, credit usage would not begin until 2021. Current usage indicates that 98 percent would be claimed by corporations and the remaining 2 percent would be claimed by personal income taxpayers.

Because this bill removes the limitation for rental real estate offsets for tax years 2019 through tax year 2023, this estimate assumes taxpayers would offset income by additional passive activity losses attributed to rental real estate activities. Because the FTB has limited data on total rental losses incurred annually, this results in an assumed additional revenue loss of $20 million in the 2021 taxable year. The incentive for taxpayers with large losses to participate in qualified low-income housing projects is not accounted for in the estimate.

Because the amendments lack language specifying the passive activity loss limitation applicable to rental real estate losses relating to low-income housing applicable to tax year 2018, California would conform to the federal limitation of $25,000 for 2018. This would result in an assumed revenue gain of $1.7 million in 2018.

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

The combined revenue impact from LIHC credit sales, credit usage, and additional passive activity losses results in a revenue loss of $5.2 million in the fiscal year 2018-19 increasing to approximately $44 million in fiscal year 2020-2021, and peaking at $180 million in fiscal year 2024-25.

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