



Analysis of Original Bill

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Bill Number: SB 1176

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Introduced: February 14, 2018

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Related Bills: See Legislative
History

Subject: Personal Exemption Credit Increase to \$700 for Each Dependent for Taxable Years Beginning on or after January 1, 2019

Summary

Under the Personal Income Tax Law (PITL), this bill would increase the dependent exemption credit.

Recommendation – No position.

Reason for the Bill

The reason for this bill is to help families by providing discretionary money that could help offset the high cost of living in California, including helping families pay for housing, food, childcare, healthcare, and transportation.

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.

Federal/State Law

Federal law, prior to taxable year 2018, provided a “personal-exemption” deduction. An exemption deduction is a reduction to adjusted gross income (AGI) to arrive at taxable income. Taxpayers were generally allowed one personal exemption for themselves, and an exemption for each claimed dependent. Each exemption was worth the same amount, and taxpayers multiplied the total number of exemptions by the current-year exemption amount. In addition to the personal exemptions, federal law also provided exemption deductions for senior, blind, and disabled taxpayers. Each dependent's taxpayer identification number (TIN) must have been provided on the federal tax return or the dependent exemption was disallowed.

For taxable year 2017, the exemption deduction was \$4,050. For taxable years beginning on or after January 1, 2018, and before January 1, 2026, federal law suspended the personal exemptions.¹ The exemption deductions will resume for taxable years beginning on or after January 1, 2026.

State Law

State law rather than providing “personal-exemption” deductions, provides “personal-exemption” tax credits. A tax credit is a dollar-for-dollar reduction to tax.

State law provides various exemption credits, including a personal exemption credit and exemption credits for dependents, blind persons, and individuals 65 or older. The exemption credit amounts for the 2017 taxable year are \$ 353 per dependent and \$ 114 per all other exemptions.

The exemption credit amounts are indexed annually for inflation. The exemption credits are not refundable and may not be carried over to future years. Exemption credits begin to phase out at federal AGI levels in excess of the amounts listed below:

Filing Status	AGI (2017)
Single/Married/RDP Filing Separate	\$187,203
Head of Household	\$280,808
Married Filing Joint/Qualifying widow(er)	\$374,411

The exemption credit amount is reduced by \$6 for every \$2,500 (\$1,250 for married filing a separate return) that the taxpayer's federal AGI exceeds the above threshold amounts, not to exceed the full amount of the credit. Taxpayers who file a joint return or who file as a surviving spouse must reduce their credit by \$12 for every \$2,500.

For taxable years beginning on or after January 1, 2015, the dependent's TIN must be provided on the California tax return or the dependent exemption credit will be disallowed.

This Bill

For taxable years beginning on or after January 1, 2019, this bill would increase the dependent exemption credit amount subject to the existing AGI limitations from \$353² to \$700 per dependent.

¹ On December 22, 2017, President Trump signed into law H.R. 1, originally known as the Tax Cuts and Jobs Act of 2017. Under Public Law (PL) 115-97, the personal exemption deduction for 2018 through 2015 is set at zero dollars (\$ 0), and then resumes for taxable years beginning on or after January 1, 2026.

² The dependent exemption credit amount of \$353 reflects the base credit of \$227 adjusted for inflation pursuant to R&TC section 17054.

For taxable years beginning on or after January 1, 2020, the increased dependent exemption amount would be indexed for inflation.

Implementation Considerations

Implementing this bill would require some changes to existing tax forms and instructions and information systems.

Technical Considerations

The annual adjustment provision provided by this bill in subparagraph (B) of paragraph (1) of subdivision (d) is unclear as to how the adjustment would be determined and the year the adjustment would commence. For clarity, it is recommended that the bill be amended to specify that the amount would be “adjusted” under subdivision (i) using “January 1, 2020,” instead of “January 1, 1989.”

Legislative History

SB 31 (Gaines, 2015/2016) would have increased the dependent credit to \$652. SB 31 failed to pass by the constitutional deadline.

SB 874 (Gaines, 2015/2016) would have increased the dependent exemption credit to \$371 per dependent. SB 874 failed to pass by the constitutional deadline.

ABX1 18 (Blumenfield, 2011/2012) would have continued the decrease in the dependent exemption credit to the same amount as the personal exemption credit for taxable years 2011 and 2012. ABX1 18 failed to pass by the constitutional deadline.

ABX3 3 (Evans, Chapter 18, Statutes of 2009) decreased the dependent exemption credit to the same amount as the personal exemption credit amount for taxable years 2009 and 2010.

SB 952 (Wyland, 2009/2010) and AB 1700 (Gaines, 2009/2010) would have repealed the reduction of the dependent exemption credit enacted in 2009, and for taxable years beginning on or after January 1, 2010, would have increased the dependent exemption credit amount to the amount it would have been if the reduction had never become operative. Both bills failed to pass by the constitutional deadline.

Other States' Information

The states surveyed include *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.

Illinois allows an exemption deduction for taxpayers and their qualifying dependents. For tax year 2017, the exemption amount was \$2,175.

Massachusetts allows a \$1,000 exemption deduction for each dependent claimed on the taxpayer's federal income tax return.

Michigan allows an exemption deduction of \$4,000 for the taxpayer, the taxpayer's spouse, and each dependent.

Minnesota allows a \$4,050 exemption deduction for each dependent claimed on the taxpayer's federal income tax return.

New York allows a \$1,000 exemption deduction for each dependent.

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 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 SB 1176 as Introduced February 14, 2018
For Taxable Years Beginning On or After January 1, 2019
Assumed Enactment after June 30, 2018

(\$ in Millions)

Fiscal Year	Revenue
2018-2019	- \$850
2019-2020	- \$1,500
2020-2021	- \$1,600

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

Revenue Discussion

Based on data from the Franchise Tax Board's PITL micro-simulation model, the amount of dependent exemption credits that taxpayers currently claim was recalculated using the proposed credit amounts, and then reduced by the amount currently claimed. The amount of additional credit each taxpayer could use would be limited by their current tax liability. As a result, the revenue loss from the increase in the dependent exemption is estimated to be \$1.5 billion in the 2019 taxable year. The exemption amounts were indexed for inflation beginning in 2020.

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

Support/Opposition

Support: None provided.

Opposition: None provided.

Arguments

Proponents: Supporters may say that this bill would increase the disposable income of California's working families and strengthen the state's economy.

Opponents: Some may argue that this bill should be broadened to increase the personal exemption credit in an effort to assist all California taxpayers rather than only those taxpayers with dependents.

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