



## Bill Analysis

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Sponsor:

Bill Number: AB 2493

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Amended: May 4, 2020

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Related Bills: See Legislative  
History

## SUBJECT

Modification to the Research Credit

## SUMMARY

This bill, under the Personal Income Tax Law (PITL) and the Corporation Tax Law (CTL), would increase the credit percentages used to calculate the California research credit for taxable years beginning on or after January 1, 2020.

In addition, the Franchise Tax Board (FTB) would be required to report specified information in accordance with Revenue and Taxation Code (R&TC) section 41.

## RECOMMENDATION

No position.

## SUMMARY OF AMENDMENTS

The May 4, 2020, amendments removed provisions of the bill that would have, under the PITL and the CTL, established a credit to be known as the Homelessness Prevention Pilot Credit Act of 2021, and replaced them with the provisions discussed in this analysis.

This is the department's first analysis of the research credit modification of the bill.

## REASON FOR THE BILL

The reason for the bill is to encourage companies to increase research and development activities for treatments, cures, and vaccines to address the global pandemic caused by COVID-19.

## ANALYSIS

For taxable years beginning on or after January 1, 2020, this bill would, under the PITL and CTL, increase the amount of the credit from 15 percent to 20 percent of the excess of qualified research expenses for the taxable year over the base amount.

In addition, this bill would, under the CTL, increase the amount of the credit for basic research payments from 24 percent to 30 percent.

Section 3 of this bill contains language that would not be included in the numbered sections of the R&TC. It provides that for purposes of R&TC section 41, with respect to the tax expenditure created by these amendments, the Legislature finds and declares that the specific goals, purposes, and objectives of this bill are as follows:

- (1) To encourage research in California.
- (2) To incentivize more research into treatments, cures, and vaccines to address COVID-19.

Despite the general disclosure provisions under the R&TC, this bill would require the FTB to provide a written report to the Senate Committee on Budget and Fiscal Review, the Assembly Committee on Budget, the Senate and Assembly Committees on Appropriations, the Senate Committee on Governance and Finance, and the Assembly Committee on Revenue and Taxation.

To measure whether the credit achieves its intended purpose, this written report would include the following information:

- (1) The number of taxpayers claiming the credit.
- (2) The average credit amount on tax returns claiming the credit.
- (3) The number of taxpayers claiming the credit in a taxable year that have not claimed the credit for a previous taxable year.

#### *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, 2020.

#### *Federal/State Law*

##### *Federal Law*

Existing federal law allows taxpayers a research credit that is combined with several other credits to form the general business credit. The credit is designed to encourage companies to increase their research and development activities.

To qualify for the credit, research expenses must qualify as an expense or be subject to amortization, be conducted in the United States, and be paid by the taxpayer. The research is required to be undertaken for discovering information that is technological in nature and its application must be intended for use in developing a new or improved business component of the taxpayer. Substantially all of the activities of the research must be elements of a process of experimentation relating to a new or improved function, performance, reliability, or quality.

The amount of federal credit is equal to 20 percent of the excess of the qualified research expenses for the taxable year over the base amount and 20 percent for basic research payments.

### *State Law*

California conforms to the federal credit with the following modifications:

- The state credit is not combined with other business credits.
- Research must be conducted in California.
- The credit percentage for qualified research in California is 15 percent versus 20 percent for the federal credit.
- The credit percentage for basic research in California is limited to corporations and is 24 percent versus 20 percent for the federal credit.
- California continues to allow the "alternative incremental credit" (AIC) calculation method with modified credit percentages, although federal law discontinued this method.
- California has yet to conform to the federal "alternative simplified credit" (ASC) calculation method.

### *Implementation Considerations*

Implementing this bill would require some changes to existing tax forms, tax form instructions, and information systems, which could be accomplished during the normal annual update.

### *Technical Considerations*

None noted.

### *Policy Considerations*

None noted.

## **LEGISLATIVE HISTORY**

AB 1564 (Pérez, 2013/2014) would have increased the credit rates of the research credit temporarily, limited the number of years that the research credit could be carried over, allowed taxpayers to sell and purchase research credits, and imposed statutory audit rules to control how the FTB audits the Research Credit. AB 1564 was held in the Assembly Appropriations Committee.

SB 235 (Wyland, 2013/2014) would have increased the California research credit rate to the federal credit rate of 20 percent, and would have increased the California AIC rates to three, four, and five percent. SB 235 failed to pass by the constitutional deadline.

## **PROGRAM BACKGROUND**

None noted.

## **FISCAL IMPACT**

This bill would not significantly impact the department's costs.

## **ECONOMIC IMPACT**

### *Revenue Estimate*

This bill would result in the following revenue loss:

Estimated Revenue Impact of AB 2493 as Amended May 4, 2020  
Assumed Enactment after June 30, 2020

(\$ in Millions)

<b>Fiscal Year</b>	<b>Revenue</b>
2020-2021	-\$55
2021-2022	-\$50
2022-2023	-\$55

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*

Based on output from the FTB's Corporate Micro-simulation Model, it is estimated that the revenue impact from the increases to the California research credit would result in a revenue loss of \$55 million for 2020 taxable year.

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

**LEGAL IMPACT**

None noted.

**APPOINTMENTS**

None noted.

**SUPPORT/OPPOSITION**

To be determined.

**ARGUMENTS**

To be determined.

**LEGISLATIVE STAFF CONTACT**

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