Analysis of Original Bill

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Sponsor:  
Phone: (916) 845-4313  
Related Bills: See Legislative History  
Bill Number: AB 2715  
Introduced: February 20, 2020

SUBJECT

California Competitiveness and Innovation Act

SUMMARY

This bill would do the following:

Provision No.1: Increase Homeowner’s Property Tax Exemption
Provision No.2: Personal Income Tax (PIT) Rate and Bracket Change
Provision No.3: Increase Renter’s Credit with Inflation Adjustment
Provision No.4: Eliminate Minimum Franchise Tax

This analysis only addresses the provisions of the bill that impact the department’s programs and operations.

RECOMMENDATION

No position

REASON FOR THE BILL

The purpose of the bill is to provide tax relief for California’s families and businesses.

ANALYSIS (ALL PROVISIONS)

Economic Impact – Summary Revenue Table ($ in Millions)

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>2020-2021</th>
<th>2021-2022</th>
<th>2022-2023</th>
</tr>
</thead>
<tbody>
<tr>
<td>Provision 1: Increase Homeowner’s Property Tax Exemption</td>
<td>0</td>
<td>+$13</td>
<td>+$27</td>
</tr>
<tr>
<td>Provision 2: Personal Income Tax (PIT) Rate and Bracket Change</td>
<td>-$18,000</td>
<td>-$12,000</td>
<td>-$13,000</td>
</tr>
<tr>
<td>Provision 3: Increase Renter’s Credit with Inflation Adjustment</td>
<td>-$160</td>
<td>-$170</td>
<td>-$180</td>
</tr>
<tr>
<td>Provision 4: Eliminate Minimum Franchise Tax</td>
<td>-$300</td>
<td>-$850</td>
<td>-$850</td>
</tr>
<tr>
<td>Total</td>
<td>-$18,460</td>
<td>-$13,007</td>
<td>-$14,003</td>
</tr>
</tbody>
</table>
Analysis Provision 1: Property Tax Exemption

This provision would increase the homeowner’s property tax exemption from $7,000 to $14,000 beginning with the lien date for the 2021-2022 fiscal year; reducing the property tax paid for purposes of the income tax deduction.

Effective/Operative Date

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

Federal/State Law

Federal Law

Federal law does not impose a property tax similar to California’s property tax.

Under current federal law, a property tax that is based on the value of the property is allowed as an itemized deduction on a personal income tax return.

State Law

Current state law requires a taxpayer who owns real estate not used for business to be assessed a tax on that property based on a specified percentage of the property’s value. The county where the property is located generally assesses this tax. The first $7,000 of the full value of a homeowners’ dwelling is exempt from that property tax.

California’s personal income tax law conforms, with modifications, to the provisions of the Internal Revenue Code allowing an itemized deduction for property tax paid, measured by the property’s value.

Implementation Considerations

Implementing this provision would not significantly impact the department’s programs and operations.

Technical Considerations

None noted.

Policy Concerns

None noted.
LEGISLATIVE HISTORY

AB 1100 (Chen, et al., 2017/2018), similar to this provision, would have increased the amount of the homeowner’s property tax exemption and the Renter’s Credit. AB 1100 failed to pass out of the Assembly Appropriations Committee.

AB 1922 (Fong, et al., 2017/2018), similar to this provision, would have increased the homeowners property tax exemption. AB 1922 failed to pass out of the Assembly Revenue and Taxation Committee.

PROGRAM BACKGROUND

None noted.

FISCAL IMPACT

This provision would not significantly impact the department’s costs.

ECONOMIC IMPACT

No Section 41 language related to AB 2715- Provision1 the Property Tax Exemption.

Revenue Estimate

This provision would result in the following revenue gain:

Estimated Revenue Impact of AB 2715-Provision1 as Introduced on February 20, 2020
For Property tax exemptions with a lien date beginning in the 2021-2022 fiscal year
Assumed Enactment after June 30, 2020

($ in Millions)

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>2020-2021</td>
<td>$0</td>
</tr>
<tr>
<td>2021-2022</td>
<td>+$13</td>
</tr>
<tr>
<td>2022-2023</td>
<td>+$27</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.
Revenue Discussion

Homeowners' Property Tax Exemption

Based on 2018 data from the Board of Equalization, the increase in the homeowner’s exemption would result in an estimated property tax savings of approximately $430 million for the 2021-2022 fiscal year. Because the increase in the exemption is not operative until lien dates beginning in fiscal year 2021-2022, it is estimated that half the impact would occur in the second half of the 2021 tax year. Based on this savings, it is estimated that itemizing taxpayers would report $210 million less in property taxes on the 2021 California tax return and $430 million less on their 2022 return, thereby increasing state taxable income. Applying an average tax rate of 6 percent would result in an estimated revenue gain of $13 million in taxable year 2021 and $27 million for taxable year 2022.

The tax year estimates are then converted to fiscal years and then rounded to arrive at the figures in the above table.

LEGAL IMPACT

None noted.

APPOINTMENTS

None noted.

SUPPORT/Opposition

To be determined.

ARGUMENTS

To be determined

Analysis Provision 2: Personal Income Tax (PIT) Rate and Bracket Change

This provision would, under the Personal Income Tax Law (PITL), modify the personal income tax rate tables to reflect the rate and bracket changes originally established by Proposition 30 in 2012. Proposition 30 included the temporary addition of three tax brackets and the increase of the top marginal tax rate in the state from 9.3 percent to 13.3 percent for California residents and part-year or non-residents, except for the head of household filing status. The changes under Proposition 30 were subsequently extended through the 2030 taxable year by Proposition 55.
This provision would do all of the following:

- Revise the PIT rate tables to reflect the rates and brackets in effect for the taxable year 2020, inclusive of indexing for inflation as of that year.
- Restart annual indexing for inflation beginning with taxable year 2021, and continue through taxable year 2030.
- Eliminate Proposition 55’s temporary rate and bracket changes by specifying an 8 percent PIT tax rate for taxable years beginning on or after January 1, 2031.

The mental health services tax would be unaffected by this provision.

Effective/Operative Date

As a tax levy, this provision would be effective immediately upon enactment. The modified PIT rate tables would be operative for taxable years beginning on or after January 1, 2020. For taxable years beginning on and after January 1, 2031, for taxable income that was subject to the Proposition 55’s temporary rate increase, the tax rate would be 8 percent.

Federal/State Law

Federal Law

Federal law imposes different income tax rates on individuals using a graduated scale. For taxable year 2018, the tax rate started at 10 percent and gradually increased to a top rate of 37 percent. For 2019, the top rate fell from 39.6 percent to 37 percent.

State Law

Existing state law imposes different PIT tax rates ranging from one percent to 12.3 percent.

Proposition 30, passed by a majority of California voters on November 6, 2012, added Section 36 to Article XIII of the California Constitution, which temporarily increased the top tax rate under Revenue and Taxation Code (R&TC) section 17041, which states the FTB shall re-compute the income tax brackets as specified, for taxable years beginning on or after January 1, 2012, and before January 1, 2019.

Proposition 55, passed by a majority of California voters on November 8, 2016, extended the tax rate increase for taxable years beginning on or after January 1, 2019, and before January 1, 2031.
Under both propositions, the 9.3 percent tax rate is increased for taxpayers that have taxable income over $250,000. The increased tax rates are 10.3 percent for the portion of taxable income that is over $250,000 but not over $300,000, 11.3 percent for the portion of taxable income that is over $300,000 but not over $500,000, and 12.3 percent for the portion of taxable income that is over $500,000, as indexed for inflation.

Under current state law an additional tax of 1 percent is imposed on the portion of an individual taxpayer’s taxable income that exceeds $1,000,000, referred to as the Mental Health Services Tax.

Implementation Considerations

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

Technical Considerations

None noted.

Policy Concerns

None noted.

LEGISLATIVE HISTORY

AB 1922 (Fong, et al., 2017/2018) similar to this provision, would have for taxable years beginning on or after January 1, 2018, with the specified exceptions, replaced the PIT tables for California residents and part-year or non-residents leaving the additional tax rates imposed by Proposition 55, as specified For taxable years beginning on or after January 1, 2031, this provision would have set the maximum tax rate at 8 percent. AB 1922 failed to pass out of the Assembly Revenue and Taxation Committee.

SB 1210 (Anderson, 2017/2018) would have created an alternate tax table for taxable income of $75,000 or less ($100,000 or less for Head of Household) that would have included a top rate of 8.8 percent. SB 1210 failed to pass out of the Senate Committee on Governance and Finance by the Constitutional deadline.

PROGRAM BACKGROUND

None noted.

FISCAL IMPACT

The department’s costs to implement this provision have yet to be determined, but are expected to be insignificant. As the bill continues to move 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 2715-Provision 2 as Introduced February 20, 2020
Assumed Enactment after June 30, 2020

($ in Millions)

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>2020-2021</td>
<td>-$18,000</td>
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<tr>
<td>2021-2022</td>
<td>-$12,000</td>
</tr>
<tr>
<td>2022-2023</td>
<td>-$13,000</td>
</tr>
</tbody>
</table>

Because the impact of current economic circumstances is unknown, this estimate is subject to change. 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

Using the FTB’s micro-simulation model, the tax liability was recalculated using the tax brackets and rates specified in this bill. This results in a revenue loss of approximately $11 billion in the 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.
Analysis Provision 3: Increase Renters Credit with Inflation Adjustment

This provision would, for taxable years on or after January 1, 2021, increase the amount of the Renter’s Credit to $120 for a qualified taxpayer using the single or married filing separate filing status and $240 for a qualified taxpayer using married filing joint, surviving spouse, or head of household filing status. The FTB would be required to annually adjust the amount of the Renter’s Credit based on the change in the California Consumer Price Index for each taxable year beginning on or after January 1, 2022.

Effective/Operative Date

As a tax levy, this provision would be effective immediately and specifically operative for taxable years beginning on or after January 1, 2021.

Federal/State Law

Federal Law

In federal law, there is no provision comparable to the California Renter’s Credit.

State Law

Current state law allows qualified renters a nonrefundable Renter’s Credit as follows:

- $120 for married filing jointly, head of household, or qualified widow or widower with an adjusted gross income (AGI) of $50,000 or less, and
- $60 for single or married filing separately with an AGI of $25,000 or less.

The credit amounts are fixed and the AGI limits are adjusted annually for inflation.

Implementation Considerations

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

Technical Considerations

None noted.

Policy Concerns

None noted.
LEGISLATIVE HISTORY

AB 1922 (Fong, et al., 2017/2018), similar to this provision, would have, among other things increased the amount of the Renter’s Credit to $120 for a qualified taxpayer using the single or married filing separate filing status and $240 for a qualified taxpayer using married filing joint, surviving spouse, or head of household filing. AB 1922 failed to pass out of the Assembly Revenue and Taxation Committee.

AB 1100 (Chen, 2017/2018) would have, among other things, contingent upon a specified appropriation, modified the Renter’s Credit. AB 1100 failed to pass out of the Assembly Appropriations Committee.

PROGRAM BACKGROUND

None noted.

FISCAL IMPACT

This provision would not significantly impact the department’s costs.

ECONOMIC IMPACT

Revenue Estimate

This provision would result in the following revenue loss:

Estimated Revenue Impact of AB 2715-Provision 3 as Introduced February 20, 2020
Assumed Enactment after June 30, 2020

($ in Millions)

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>2021-2022</td>
<td>-$160</td>
</tr>
<tr>
<td>2022-2023</td>
<td>-$170</td>
</tr>
<tr>
<td>2023-2024</td>
<td>-$180</td>
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</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.
Revenue Discussion

Based on the FTB Renter’s Credit data, the amount of credit for taxpayers currently claiming the credit 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 available Renter’s Credit is estimated to be $130 million in 2017. The estimate was then adjusted to reflect changes in the economy over time, resulting in an estimated $160 million revenue loss in the 2021 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.

Analysis Provision 4: Eliminate Minimum Franchise Tax (MFT)

This provision, under the Corporation Tax Law (CTL), would specify that the MFT applies to taxable years ending before January 1, 2021.

Effective/Operative Date

As a tax levy, this provision would be effective immediately and operative tax for taxable years beginning on or after January 1, 2020.

Federal/State Law

Federal Law

Federal law does not require that a corporation pay a minimum tax.
State Law

Under existing state law, corporations that incorporate, qualify, or start doing business in California, are subject to the minimum franchise tax. The minimum franchise tax is assessed if it is greater than the tax measured by the corporation’s net income. A corporation is subject to the minimum franchise tax until the corporation dissolves or withdraws or, if later, until it stops doing business in California. For taxable years beginning on or after January 1, 1997, the measured tax is imposed on net income at a rate of 8.84 percent. Thus under current law, only corporations with net income less than approximately $9,040 pay the minimum franchise tax because their measured tax would be less than $800 ($9,039 \times 8.84\% = $799).

Every corporation that incorporates or qualifies to do business in this state on or after January 1, 2000, is exempt from the minimum franchise tax for its first taxable year. This exemption is inapplicable to a corporation that reorganizes solely for the purpose of avoiding payment of its minimum franchise tax. The first taxable year exemption also does not apply to limited partnerships (LPs); limited liability companies (LLCs) not classified as corporations, limited liability partnerships (LLPs), charitable organizations, regulated investment companies (RICs), real estate investment trusts (REITs), real estate mortgage investment conduits (REMICs), and financial asset securitization investment trusts (FASITs).

In general, under the CTL, corporations, Subchapter S corporations, RICs, REITs, REMICs, and FASITs are subject to the $800 minimum franchise tax.

In general, under the Personal Income Tax Law (PITL), LPs, LLCs not classified as corporations, and LLPs, are subject to an annual tax that is determined by reference to the MFT.

For taxable years beginning on or after January 1, 2020, an LLC or corporation that is a small business solely owned by a deployed member of the United States (U.S.) Armed Forces is not subject to the annual or minimum franchise tax for any taxable year that the owner is deployed and the LLC or corporation operates at a loss or ceases operation. The minimum franchise tax amount for the second tax year and all subsequent tax years is $800.

Under R&TC section 41, legislation that would create a new tax expenditure, which includes a credit, deduction, exclusion, exemption, or any other tax benefit as provided for by the state, is required to include specific goals, purposes, objectives, and performance measures to allow the Legislature to evaluate the effectiveness of the tax benefit.
Implementation Considerations

The department has identified the following concerns. Department staff is available to work with the author’s office to resolve these and other concerns that may be identified.

The amount of the MFT applicable to taxable years beginning on or after January 1, 2021, is unclear. To avoid disputes between taxpayers and the department, and to ensure consistency with the author’s intent, this provision should be amended.

Under Revenue and Taxation Code (R&TC) section 41, legislation that would create a new tax expenditure, which includes a credit, deduction, exclusion, exemption, or any other tax benefit as provided for by the state, is required to include specific goals, purposes, objectives, and performance measures to allow the Legislature to evaluate the effectiveness of the tax benefit. This bill should be amended to satisfy the R&TC section 41 requirements.

Technical Considerations

None noted.

Policy Concerns

This provision would provide a tax benefit for corporations under the Corporation Tax Law that would be unavailable to other business entities under the Personal Income Tax Law, such as limited partnerships, limited liability companies not classified as corporations, limited liability partnerships, charitable organizations, regulated investment companies, real estate investment trusts, real estate mortgage investment conduits, financial asset securitization investment trusts, and qualified Subchapter S subsidiaries. Thus, this provision would provide differing treatment based solely on classification.

This provision lacks a sunset date, which is generally provided to allow periodic review of the effectiveness of income tax law changes by the Legislature.

LEGISLATIVE HISTORY

AB 1922 (Fong, et al., 2017/2018) would have among other things, eliminated the MFT of $800 for all corporations by repealing the minimum tax provisions under the CTL. AB 1922 failed to pass out of the Assembly Revenue and Taxation Committee.

AB 166 (Cook, 2011/2012) would have eliminated the MFT. AB 166 failed to pass out of the Assembly Revenue and Taxation Committee.
PROGRAM BACKGROUND

None noted.

FISCAL IMPACT

The department’s costs to implement this provision 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 2715-Provision 4 as Introduced February 20, 2020
Assumed Enactment after June 30, 2020

($ in Millions)

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>2020-2021</td>
<td>-$300</td>
</tr>
<tr>
<td>2021-2022</td>
<td>-$850</td>
</tr>
<tr>
<td>2022-2023</td>
<td>-$850</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.

Revenue Discussion

The provisions of this bill repeal the minimum franchise tax for corporations. Based on the data from the FTB for tax years 2017, it is estimated that for taxable year 2021 the revenue loss from the proposed changes to the minimum franchise tax for C and S corporations would be approximately $800 million. The estimated revenue loss consists of the minimum franchise tax that would no longer be paid offset by calculated measured franchise tax. This is determined by multiplying the C or S Corporation’s net taxable income by their current tax rate.

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 provided.

SUPPORT/OPPOSITION

To be determined.

ARGUMENTS

To be determined.

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