



## Summary Analysis of Amended Bill

Author: Jones-Sawyer, et al.      Sponsor:      Bill Number: AB 37  
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Attorney: Shane Hofeling      Related Bills: See Prior Analysis

**Subject:** Personal Income Tax Deduction and Credits Related to Commercial Cannabis Activities

### Summary

This bill would, under the Personal Income Tax Law (PITL), specify that the federal disallowance of tax expenditures related to the illegal sale of drugs would not apply to licensees engaged in the trade or business of commercial cannabis activities in the State.

**Recommendation – No position.**

### Summary of Amendments

The August 30, 2019, amendments made minor technical changes and modified the uncodified reporting requirements.

As a result of the August 30, 2019, amendments, a new “Implementation Consideration” was identified and two of the implementation concerns and the technical concerns identified in the department’s analysis of the bill as amended June 13, 2019, were resolved. Except for the “This Bill,” “Implementation Considerations,” “Technical Considerations,” and “Fiscal Impact” sections, the remainder of the department’s analysis of the bill as amended on June 13, 2019, still applies. The “Effective/Operative Date” and “Economic Impact” sections have been restated below for convenience.

### 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, and before January 1, 2025.

## **This Bill**

This bill would, under the PITL, for taxable years beginning on or after January 1, 2020, and before January 1, 2025, allow licensees engaged in commercial cannabis activity, to deduct expenses and claim tax credits, related to that trade or business.

“Commercial cannabis activity” and “licensee” would have the same meaning as specified in Section 26001 of the Business and Professions Code.

In uncodified law, this bill would require the Franchise Tax Board (FTB) to:

- Collect data relating to the number and total dollar amounts of deductions and credits claimed by licensees engaged in commercial cannabis activity that are subject to the PITL.
- Report the required data to the Legislature on or before July 31 of each calendar year in which either the deductions or credits are allowed, as specified.<sup>1</sup>

## **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.

The department would be required to collect data and report on the number and total dollar amount of deductions and credits claimed under the terms of this bill. Collecting this data would require the department to change its systems, forms, and processes, which could be costly.

Personal income tax returns may be filed, with extension, until October 15. The department generally processes returns within six months of receipt. If the author’s intent is to have each report contain complete information for the taxable year, the due date of the report should be changed. For instance, for tax year 2020, the return due date, with extension, would be October 15, 2021. The department would complete processing of these returns by April 2022. Thus, the earliest that data from these individual returns could be included in a report would be approximately June 2022.

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<sup>1</sup> Government Code section 9795 generally specifies to whom reports to the Legislature must be provided and the required format.

## **Fiscal Impact**

Staff estimates a cost of approximately \$17,000 for fiscal year 2020-2021 and \$29,000 for fiscal years 2021-2022 and thereafter for resources required to capture return data.

## **Economic Impact**

### Revenue Estimate

This bill as amended on August 30 2019, would have a revenue impact on the general fund, but the amount is unknown.

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

Absent the availability of FTB data, the department identified a review article issued by the University of California Agricultural Issues Centers (AIC) that examined six different studies on the cannabis market and its potential market size. The AIC review article indicated that the commercial cannabis activities market could be valued between \$4 billion and \$11 billion in California.

Until taxpayers file their 2018 taxable year returns, the form of business ownership will remain unknown. For purposes of this estimate, it is assumed that these entities would operate under the PITL, e.g., a sole proprietorship or partnership. Using income and expense data in the AIC report it is assumed that ordinary and necessary business expenses would be approximately 20 percent of sales. As a result, every \$1 billion in retail market sales would result in an estimated additional \$200 million in deductions claimed resulting in an estimated revenue loss of \$13 million per \$1 billion in PITL retail sales.

In addition to expense deductions, this bill would allow commercial cannabis activities to claim tax credits. Because the amount and types of credits these businesses would claim is unknown, the additional revenue loss attributable to credits is unknown.

## **Legislative Staff Contact**

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