STATE OF CALIFORNIA
Franchise Tax Board

Summary Analysis of Amended Bill

Author: Rubio	Sponsor:	Bill Number: SB 775
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Subject: Exempt Organizations/Mutual Ditch or Irrigation Companies

Summary

Under the Corporation Tax Law, this bill would exempt certain mutual ditch or irrigation companies from tax.

Recommendation – No position.

Summary of Amendments

The July 3, 2019, amendments added a sunset date, additional qualifying requirements, administrative requirements for the State Water Resources Control Board (SWRCB) and, in off-code language, added department reporting requirements.

The July 3, 2019, amendments resolved the previously identified implementation considerations and policy concerns, however an additional implementation consideration was identified. Except for the "Effective/Operative Date," "This Bill," "Implementation Considerations," "Fiscal Impact," and "Policy Concerns," sections, the remainder of the department's analysis of the bill as amended May 7, 2019, still applies. The "Economic Impact" section has been restated for convenience.

Effective/Operative Date

This bill would be effective January 1, 2020, and specifically operative for taxable years beginning on or after January 1, 2019, and before January 1, 2024.

This Bill

For taxable years beginning on or after January 1, 2019, and before January 1, 2024, this bill would generally exempt mutual ditch and irrigation companies that operate a public water system from corporate income and franchise taxes, unless the ditch and irrigation company (company) fails to meet certain requirements as specified in either, or both, the Corporations Code and the Health and Safety Code, or fails to provide information to a local agency formation commission.

The companies must also adopt policies to comply with open meeting and record accessibility requirements, and submit these adopted policies and a certification of compliance to the Division of Drinking Water of the SWRCB by June 30, 2020, and by June 30th of each year annually thereafter.

The bill would then require the Division of Drinking Water of the SWRCB to submit a list of the companies that have not complied with the open meeting and record accessibility requirements to the Franchise Tax Board (FTB or the department) by September 30, 2020, and by September 30th of each year annually thereafter.

Generally, any funding provided by the SWRCB to a company operating a public water system is excluded from the definition of gross income. Such funding would have no impact on the company's tax-exempt status.

In addition, annually, this bill would require the department to determine the number of corporations that have applied for the exemption and calculate the lost tax revenue due to the exemption.

This provision will remain in effect until December 1, 2024, and as of that date is repealed.

Implementation Considerations

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

This bill provides that this provision will remain in effect until December 1, 2024, and as of that date is repealed. Accordingly, any entity that receives tax exemption by operation of this bill would no longer be exempt after the repeal date. These entities would need to qualify for exemption under a different tax-exempt criteria, or would become a taxable entity. If this does not reflect the author's intent, consider amending the bill.

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.

Fiscal Impact

Staff estimates a cost of approximately $175,000 in fiscal year 2019/2020 (and ongoing costs of $280,000) to develop, program, and test revisions to existing systems for this bill. The department will pursue a budget change proposal if necessary.

Economic Impact

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of SB 775 as Amended July 3, 2019
Assumed Enactment after June 30, 2019

Fiscal Year	Revenue
2019-2020	-$800,000
2020-2021	-$700,000
2021-2022	-$700,000

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 Internal Revenue Service and FTB exempt organization data, it was estimated that in 2019 companies would owe approximately $700,000 in taxes to California. It is assumed that all companies would meet the requirements specified in the bill. As a result, the revenue loss would be $700,000 in the 2019 taxable year.

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

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