



## Bill Analysis

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Sponsor:

Bill Number: AB 249

Related Bills: See Legislative  
History

Amended: January 03, 2022

### SUBJECT

Modification to the California Research Tax Credit

### SUMMARY

This bill would, under Personal Income Tax Law (PITL) and Corporation Tax Law (CTL) increase the amount of research credit to 20 percent of the excess of the qualified research expenses over the base amount for each taxable year beginning on or after January 1, 2022, and before January 1, 2027. The bill would also under CTL increase the amount of the credit for basic research payments to 30 percent for each taxable year beginning on or after January 1, 2022, and before January 1, 2027.

In addition, the Franchise Tax Board (FTB) would be required to report specified information in accordance with Revenue and Taxation Code (RTC) section 41 no later than July 31, 2023.

### RECOMMENDATION

No position.

### SUMMARY OF AMENDMENTS

The January 3, 2022, amendments modified the operative date and added a sunset provision for increasing the amount of research credit to 20 percent of the excess of the qualified research expenses over the base amount under the PITL and CTL; modified the operative date and added sunset provision for increasing the amount of the credit for basic research payments to 30 percent; added a due date for the FTB reporting requirement in accordance with RTC section 41.

### REASON FOR THE BILL

The purpose of this bill is to increase the research tax credit percentage to encourage research activity in California, and incentivize more research into treatments, cures, and vaccines to address the global pandemic caused by COVID-19.

## **ANALYSIS**

For taxable years beginning on or after January 1, 2022, and before January 1, 2027, 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 by conforming to the federal 20 percent amount.

In addition, for taxable years beginning on or after January 1, 2022, and before January 1, 2027, this bill would, under the CTL, increase the amount of the credit for basic research payments from 24 percent to 30 percent.

After these provisions expire, the credit percentages would revert back to the existing credit percentages discussed below.

Furthermore, this bill would make several nonsubstantive technical changes to the language of the research credit.

Section 3 of this bill provides that for purposes of RTC 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:

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

This bill would require the FTB to provide a written report, no later than July 31, 2023, 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:

- The number of taxpayers claiming the credit.
- The average credit amount on tax returns claiming the credit.
- 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 operative for taxable years beginning on or after January 1, 2022. The increased credit percentages would be specifically operative for taxable years beginning on or after January 1, 2022, and before January 1, 2027.

### *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, 20 percent for basic research payments, and 20 percent of amounts paid or incurred for carrying on a trade or business to an energy research consortium for energy research.

#### *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 expenses in California is 15 percent versus 20 percent for the federal credit.
- The credit percentage for basic research payments 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*

None noted.

#### *Technical Considerations*

None noted.

### *Policy Considerations*

None noted.

### **LEGISLATIVE HISTORY**

AB 2493 (Choi, 2019/2020) was substantially similar to this bill. AB 2493 was held in Committee on Revenue and Taxation without further action.

AB 653 (Pérez, et al., 2013/2014) would have provided temporary incremental increases to the California research credit rates. AB 653 was held in the Assembly Appropriations Committee.

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.

AB 2330 (Mullin, et al., 2013/2014) would have conformed to the ASC for taxable years beginning on or after January 1, 2015, and before January 1, 2022, eliminated the AIC for taxable years beginning on or after January 1, 2015, and conformed to recent federal rule changes relating to acquisitions and aggregations of expenditures. AB 2330 was held in the Assembly Appropriations Committee.

SB 235 (Wyland, et al., 2013/2014) would have increased the California research credit percent to the federal credit percent of 20 percent, and would have increased the California AIC to three, four, and five percent. SB 235 was held in the Senate Governance and Finance Committee.

### **PROGRAM BACKGROUND**

Congress enacted the federal research credit in 1981 to stimulate increased research activities and innovation in the United States. California enacted a similar research credit in 1987 by conforming, with modifications, to the federal credit, for research conducted in this state.

### **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.

## **ECONOMIC IMPACT**

### *Revenue Estimate*

This bill would result in the following revenue loss:

Estimated Revenue Impact of Assembly Bill 249 as Amended January 3, 2022.  
Assumed Enactment after June 30, 2022

(\$ in Millions)

<b>Fiscal Year</b>	<b>Revenue</b>
2021-2022	-\$100
2022-2023	-\$100
2023-2024	-\$100

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.

## **LEGAL IMPACT**

None noted.

## **APPOINTMENTS**

None noted.

## **SUPPORT/OPPOSITION**

To be determined.

## **ARGUMENTS**

To be determined.

## **LEGISLATIVE CONTACT**

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