



Bill Analysis

Author: Cooley, et al.

Sponsor:

Bill Number: AB 820

Related Bills: See Legislative
History

Amended: January 3 and
January 12, 2022

SUBJECT

Income and Sales Factor Exclusion for Interest - Banks and Financials

SUMMARY

This bill would do the following:

Provision No. 1 ~ Income Exclusion of Qualified Interest Income

This provision, under the Corporation Tax Law (CTL), would allow banks and financial corporations, which generate business income solely from or attributable to sources within California, a gross income exclusion for qualified interest income, as provided, that is generated from qualified loans made to California small businesses.

Provision No. 2 ~ Sales Factor Exclusion of Qualified Interest Income

This provision, under the CTL, would provide that banks and financial corporations, which generate business income from or attributable to sources within and without California, would also exclude the interest from the sales factor.

Provision No. 3 ~ FTB Reporting Requirements

This provision would require the Franchise Tax Board (FTB) to provide any available data related to the provisions of this bill to the Legislative Analyst's Office (LAO), as provided.

RECOMMENDATION

No position.

SUMMARY OF AMENDMENTS

The January 3, 2022, amendments changed the operative date, amended the definition of a "full-time equivalent employee," changed the term "interest revenue" to "interest income," added a comparison date for the 10% or more net loss test, added a repeal date, extended the Section 41 reporting due date to December 1, 2028, and made other nonsubstantive changes.

These amendments resolved all of the implementation and technical considerations as discussed in the department's analysis of the bill as amended on March 18, 2021. In addition, another technical and policy consideration have been identified.

The January 12, 2022, amendments added two coauthors and changed the definition of a "qualified loan" to exclude any loan backed by any local, state, or federal government funds.

REASON FOR THE BILL

The reason for the bill is to encourage financial institutions to provide loans to small businesses adversely impacted by the COVID-19 Pandemic.

Economic Impact – Summary Revenue Table (\$ in Millions) (All Provisions)

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of AB 820 as Amended January 12, 2022
Assumed Enactment after June 30, 2022

(\$ in Millions)

Fiscal Year	Revenue
2022-2023	-\$330
2023-2024	-\$280
2024-2025	-\$260

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.

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, 2022, and before January 1, 2027.

ANALYSIS

Analysis Provision 1:

Income Exclusion of Qualified Interest Income (Section 1)

For taxable years beginning on or after January 1, 2022, and before January 1, 2027, Provision 1 of this bill, under the CTL, would provide a qualifying bank or financial corporation a gross income exclusion for the amount of qualified interest income generated by qualified loans made to qualified small businesses.

For purposes of this provision, the following definitions would apply:

- A) "Qualified interest income" would mean interest income that a qualified taxpayer generates on a qualified loan during the taxable year.
- B) "Qualified loan" would mean a loan of \$1,000,000 or less made by the qualified taxpayer to a qualified small business on or after March 15, 2020, but prior to January 1, 2025. However, a "qualified loan" would not include any loan that is backed by any local, state, or federal government funds.
- C) "Qualified small business" would mean a business that meets the following requirements:
 - 1) Has 50 or fewer full-time or full-time equivalent employees on the date of the loan application.
 - i. "Full-time equivalent" would mean either of the following:
 - a. In the case of a full-time employee paid hourly wages, the total number of hours worked for the qualified taxpayer by the employee, not to exceed 2,000 hours per employee, divided by 2000.
 - b. In the case of a salaried full-time employee, the total number of weeks worked for the qualified taxpayer by the employee divided by 52.
 - 2) Experienced an annual loss in net income of 10% or more based on net income from January 1, 2020, to December 31, 2020, inclusive, compared to net income from January 1, 2021, to December 31, 2021, inclusive.
 - 3) Is located in the state.
- D) "Qualified taxpayer" would mean a bank or financial corporation, as defined under existing provisions of the Revenue and Taxation Code (RTC), that generates business income that is solely derived from or attributable to sources within this state, and is therefore not subject to apportionment.

This provision would remain in effect until December 1, 2027, and as of that date would be repealed.

Federal/State Law

Existing federal and state laws provide that gross income includes all income from whatever source derived, including compensation for services, business income, gains from property, interest, dividends, rents, and royalties, unless specifically excluded.

Existing federal and state laws provide that certain types of income are excluded from gross income, such as amounts received as a gift or inheritance, certain compensation for injuries and sickness, qualified scholarships, educational assistance programs, foster care payments, and interest received on certain state or federal obligations.

In addition, under existing state law, a "bank" generally includes a national banking association and any "bank" operated by any receiver, liquidator, referee, trustee or other officers or agents appointed by any court, or an assignee for the benefit of creditors. A "financial corporation" generally means a corporation that predominantly deals in money or moneyed capital in substantial competition with the business of national banks.

Implementation Considerations

None noted.

Technical Considerations

The department has identified the following technical consideration, and is available to work with the author's office to resolve this and other considerations that may be identified.

For consistency of terminology, the following changes are recommended in Section 24313.5(b):

(A) In the case of a full-time employee paid hourly wages, the total number of hours ~~worked~~*employed* for the qualified taxpayer by the employee, not to exceed 2,000 hours per employee, divided by 2000.

(B) In the case of a salaried full-time employee, the total number of weeks ~~worked~~*employed* for the qualified taxpayer by the employee divided by 52.

Policy Considerations

The author may wish to clarify whether employees working remotely outside of California would be included in the calculation of full-time equivalent employees.

LEGISLATIVE HISTORY

No legislation similar to this provision of the bill has been identified.

PROGRAM BACKGROUND

None noted.

LEGAL IMPACT

None noted.

Analysis Provision 2:

Sales Factor Exclusion of Qualified Interest Income (Section 2)

Provision 2 of this bill, under the CTL, for taxable years beginning on or after January 1, 2022, and before January 1, 2027, would provide that for qualifying banks or financial corporations the amount of qualified interest income generated by qualified loans made to qualified small businesses would also be excluded from the sales factor.

For purposes of this provision, the definition for “qualified loan,” and “qualified small business” from the above Provision 1 Analysis above would also apply for this Provision 2:

- A) “Qualified interest income” would mean interest income that a qualified taxpayer generates on a qualified loan during the taxable year and that would be subject to apportionment.
- B) “Qualified taxpayer” would mean a bank or financial corporation that generates income that is derived from or attributable to sources within and without this state, and is therefore subject to apportionment.

This provision would remain in effect until December 1, 2027, and as of that date would be repealed.

Federal/State Law

Federal Law

No comparable provision in federal law.

State Law

Under California law, corporations deriving income from sources both within and outside California are required to measure their tax liability by reference to their income derived from or attributable to sources within California. To determine the portion of total income that is attributable to California, the apportionment and allocation method is used.

In addition, under California law, all affiliated United States and foreign entities comprising a single trade or business are viewed for certain purposes as a whole called a "unitary group." The business income of all the affiliates that comprise a unitary group is apportioned and reported to California on a single report known as the "combined report." The apportionment method only applies when a corporation operating in California derives income from sources both within and outside California. The apportionment method does not apply to a corporation operating wholly within California. In addition, a corporation would only be required to file in a "combined report" if it is unitary with another corporation, and at least one of the unitary corporations derives income from sources both within and outside California.

The apportionment method uses a formula to calculate the amount of a unitary group's total income that was generated from the unitary group's activities in California. This formula is comprised of a single sales factor that measures the activity of a unitary group in the state. There is an exception for qualified business activities in agriculture, extraction, savings and loans, and banking. The apportionment formula for these businesses is comprised of four components that measure the activity of the unitary group in the state: property, payroll, and double-weighted sales. The unitary group's California business income is then apportioned among the members that are taxable in California. Each member retains a separate tax identity and liability.

Implementation Considerations

None noted.

Technical Considerations

The department has identified the following technical consideration, and is available to work with the author's office to resolve this and other considerations that may be identified.

For consistency of terminology, the following changes are recommended in Section 25128.1(b):

(A) In the case of a full-time employee paid hourly wages, the total number of hours ~~worked~~*employed* for the qualified taxpayer by the employee, not to exceed 2,000 hours per employee, divided by 2000.

(B) In the case of a salaried full-time employee, the total number of weeks ~~worked~~*employed* for the qualified taxpayer by the employee divided by 52.

Policy Considerations

The author may wish to clarify whether employees working remotely outside of California would be included in the calculation of full-time equivalent employees.

LEGISLATIVE HISTORY

No legislation similar to this provision of the bill has been identified.

PROGRAM BACKGROUND

None noted.

LEGAL IMPACT

None noted.

ANALYSIS

Analysis Provision 3:

FTB Reporting Requirements (Section 3)

For purposes of Section 41, the detailed performance indicators to measure whether the tax benefits of the bill meet the goals and objectives of the bill include the number of banks and financial corporations excluding qualified interest income from gross income, the number of banks and financial corporations excluding qualified interest income from the apportionment factor, and the amount of qualified interest income excluded from business income apportionment factor.

The LAO would be required to collaborate with the FTB to analyze whether the tax benefits meet the goal, purpose, and objective of this bill. The LAO may request information from the FTB, and the FTB would be required to provide any available data as requested by the LAO. The LAO would report their analysis to the Legislature, in compliance with Government Code section 9795, Reports to the Legislature, by December 1, 2028.

To allow the necessary FTB reporting to the LAO, the bill provides an exception to the provisions of RTC section 19542, disclosure prohibition of confidential taxpayer information.

Federal/State Law

Existing California state laws require the FTB to report certain information to the California Legislature or other state agencies, as directed. Additionally, for both federal and state purposes, the disclosure of any confidential taxpayer information is prohibited, except as specifically authorized by statute.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

No legislation similar to this provision of the bill has been identified.

PROGRAM BACKGROUND

None noted.

LEGAL IMPACT

None noted.

FISCAL IMPACT (All Provisions)

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.

APPOINTMENTS (All Provisions)

None provided.

SUPPORT/OPPOSITION (All Provisions)

Support

As per the Assembly Revenue and Taxation Committee analysis of AB 820, dated January 7, 2022, the following organizations support this bill: Building Owners and Managers Association; California Bankers Association; California Business Properties Association; California Business Roundtable; California Retailers Association; El Dorado County Chamber of Commerce; Elk Grover Chamber of Commerce; Five STAR Bank; Folsom Chamber of Commerce; NAIOP of California; National Federation of Independent Business, California; Rancho Cordova Chamber of Commerce; Roseville Chamber of Commerce; United Chamber Advocacy Network; Yuba Sutter Chamber of Commerce.

Opposition

As per the same analysis, dated January 7, 2022, the California School Boards Association opposes the bill.

ARGUMENTS (All Provisions)

None noted.

LEGISLATIVE CONTACT

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