Bill Analysis

Author: Committee on Budget and Fiscal Review	Sponsor:	Bill Number: SB 113
	Related Bills: See Legislative History	Introduced: January 8, 2021 Amended: February 2, 2022

SUBJECT

COVID-19 Economic Relief Budget Trailer Bill

SUMMARY

This bill would do the following:

Provision No. 1 - Credits Reducing Regular Tax Below Tentative Minimum Tax (TMT) and Credit Ordering:

Sections 6 and 26 of the bill would, under the Personal Income Tax Law (PITL), allow the pass-through entity elective tax (PTEET) credit to reduce regular tax below TMT and would make changes to the order of credits allowed to be taken against the "net tax." In addition, this provision would make other nonsubstantive technical changes.

Provision No. 2 - Repeal of Business Tax Credit Limitation for 2022:

Sections 7, 16, and 25 of the bill would, under the PITL and Corporation Tax Law (CTL), repeal the business tax credit limitation for taxable years beginning on or after January 1, 2022.

Provision No. 3 - PTEET Election and Credit Modifications:

Sections 8, 14, 15, and 26 of the bill would, for purposes of the PTEET election under the Small Business Relief Act (SBRA), modify the definition of "qualified net income" to include guaranteed payments and would expand the definition of a "qualified entity" to allow the entity's partners, shareholders, or members to include a partnership.

In addition, for purposes of the PTEET credit, under the PITL, the provision would modify the definition of "qualified amount" on which the credit is based to include guaranteed payments, and would modify a "qualified taxpayer" eligible to claim the credit to include certain disregarded limited liability companies (LLCs).

Provision No. 4 - Gross Income Exclusion of Water and Wastewater System Payments:

Sections 9, 19, and 23 of the bill would, under the PITL and CTL, provide a gross income exclusion for certain water assistance received under the California Water and Wastewater Arrearage Payment Program.

Provision No. 5 - Gross Income Exclusion of the California Arrearage Payment Program (CAPP):

Sections 10, 20, and 24 of the bill would, under the PITL and CTL, provide a gross income exclusion for utility payment assistance received under the CAPP.

Provision No. 6 - Gross Income Exclusion of Restaurant Revitalization Grants (RRG):

Sections 11, 17, 22, and 27 of the bill would, under the PITL and CTL, provide a gross income exclusion for RRG. This provision would also conform to the allowance of deductions and treatment of tax basis and other tax attributes relating to amounts excluded.

Provision No. 7 – Gross Income Exclusion of Shuttered Venue Operator Grants (SVOG):

Sections 12, 18, 22, and 27 of the bill would, under the PITL and CTL, provide a gross income exclusion for SVOG. This provision would also conform to the allowance of deductions and treatment of tax basis and other tax attributes relating to amounts excluded.

Provision No. 8 - Repeal of Net Operating Loss (NOL) Deduction Suspension for 2022:

Sections 13, 21, and 25 of the bill would, under the PITL and CTL, repeal the suspension of the NOL deduction for the 2022 taxable year.

Repeal of the Motion Picture Sales and Use Tax Credit for 2022

Section 4 of the bill would, under the Sales and Use Tax (SUT) Laws, modify the irrevocable election to apply motion picture tax credits against sales and use taxes, in lieu of income and franchise taxes, limited to $5,000,000, from taxable years beginning on or after January 1, 2020, and before January 1, 2023, to taxable years beginning on or after January 1, 2020, and before January 1, 2022. This election and SUT credit is administered by the California Department of Tax and Fee Administration.

RECOMMENDATION

No position.

SUMMARY OF AMENDMENTS

The February 2, 2022, amendments removed intent language relating to the Budget Act of 2021, and replaced it with the provisions discussed in this analysis.

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

REASON FOR THE BILL

The reason for the bill is to make various statutory changes related to implementing the 2021 Budget Act.

ANALYSIS

Economic Impact – Summary Revenue Table ($ in Millions)

Fiscal Year	2021-2022	2022-2023	2023-2024
Provision No. 1 - Credits Reducing Regular Tax Below TMT and Credit Ordering	-$4.5	$210	$110
Provision No. 2 – Repeal of Business Tax Credit Limitation for 2022	-$1,200	-$2,300	-$5.4
Provision No. 3 - PTEET Election and Tax Credit Modifications	$60	$60	$50
Provision No. 4 – Gross Income Exclusion of Water and Wastewater System Payments	N/A	N/A	N/A
Provision No. 5 – Gross Income Exclusion of the CAPP	N/A	N/A	N/A
Provision No. 6 – Gross Income Exclusion of RRG	-$110	-$120	-$95
Provision No. 7 –Gross Income Exclusion of SVOG	-$47	-$50	-$41
Provision No. 8 – Repeal of NOL Deduction Suspension for 2022**	-$800	-$1,300	$170

**The revenue estimate for Provision No. 8 includes the impact of the interaction between Provision No. 2 and Provision No. 8.

FISCAL IMPACT

Implementing this bill would not significantly impact the department's programs and operations.

Analysis Provision No. 1: Credits Reducing Regular Tax Below TMT and Credit Ordering (Sections 6 and 26)

Under the PITL, this provision would specify that for taxable years beginning on or after January 1, 2021, the PTEET credit (relating to the elective tax credit under the SBRA) would be allowed to reduce the "net tax" below the TMT. Also, for taxable years beginning on or after January 1, 2022, this provision would change the order of the credits allowed to be taken against the "net tax," by prescribing that the PTEET credit be taken after credits for taxes paid to other states, and before credits that contain refundable provisions but not carryover provisions.

Other technical changes regarding repeal dates of prior credits would also be made to specify the effective dates of those technical changes.

For purposes of complying with Revenue and Taxation Code (RTC) section 41, the provision specifies that the goal of the tax expenditure is to provide tax relief to small businesses facing unprecedented economic hurdles due to COVID-19.

Effective/Operative Date

As a provision within a bill providing for appropriations relating to the Budget Bill, this provision would be effective immediately upon enactment and specifically operative as follows: the amendments allowing the PTEET credit to reduce tax below TMT would be operative for taxable years beginning on or after January 1, 2021; and the amendments relating to the subdivision changing the order of the tax credits and other technical changes would be operative for taxable years beginning on or after January 1, 2022.

Federal/State Law

Federal Law

General business credits allowed for any tax year are limited to the excess of a taxpayer's "net income tax" over the greater of: (1) the TMT for the tax year, or (2) 25% of the amount of the taxpayer's "net regular tax" that exceeds $25,000. In addition, the empowerment zone employment credit, eligible small business credits, and other "specified credits" have various rules for limiting the usage of credits. (Internal Revenue Code (IRC) section 38(c), as in effect on January 1, 2015.)

State Law

Current state law provides an order for credits to be allowed against the "net tax" as follows:

(1) Credits that do not contain carryover or refundable provisions, except those described below in (4) and (5);
(2) Credits that contain carryover provisions but do not contain refundable provisions, except for those that are allowed to reduce "net tax" below the TMT;
(3) Credits that contain both carryover and refundable provisions;
(4) The minimum tax credit allowed by Section 17063 (relating to the alternative minimum tax);
(5) Credits that are allowed to reduce "net tax" below the TMT;
(6) Credits for taxes paid to other states allowed by Chapter 12 (commencing with Section 18001); and
(7) Credits that contain refundable provisions but do not contain carryover provisions.

Current state law provides a general rule that tax credits imposed under the PITL may not reduce regular tax below TMT, unless specifically provided otherwise. There are numerous credits listed that are allowed to reduce the "net tax" below the TMT, such as solar energy credits, the College Access Tax Credit, and the California Competes Tax Credit. Credits may be carried over until used completely or for the specified carryover period, even if a credit is repealed.

PTEET Credit

Under the PITL, for taxable years beginning on or after January 1, 2021, and before January 1, 2026, a qualified taxpayer, who is a partner, shareholder or member of a qualified entity under the SBRA that makes an annual election to pay the elective tax is allowed a tax credit. The amount of the credit is equal to 9.3% of the pro rata or distributive share of income subject to tax under the PITL included in the qualified net income of the electing qualified entity.

Any unused credit may be carried over for five years, until exhausted. However, the credit may not be used to reduce the TMT.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

AB 150 (Committee on Budget, Chapter 82, Statutes of 2021), amongst other items, created the SBRA, which for taxable years beginning on or after January 1, 2021, and before January 1, 2026, allows entities taxed as a partnership or S corporation to pay an additional elective tax at the entity level. In addition, AB 150 enacted the PTEET credit, which allows a qualified taxpayer, who is an owner of a qualified entity that makes an annual election to pay an additional elective tax, the PTEET credit in an amount equal to 9.3% of the qualified taxpayer's pro rata or distributive share, as applicable, of the qualified net income subject to the election made by an electing qualified entity under the SBRA.

PROGRAM BACKGROUND

None noted.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue impact:

Estimated Revenue Impact of SB 113 Provision No. 1 as Amended on February 2, 2022
Assumed Enactment Prior to April 30, 2022

($ in Millions)

Fiscal Year	Revenue
2021-2022	-$4.5
2022-2023	$210
2023-2024	$110

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

This provision would allow entities taxed as a partnership or an S corporation to elect to pay an additional tax of 9.3% on their business income. This additional tax would reduce the amount of income the owners of those businesses, would have to report for federal tax purposes. In addition, owners would receive a credit against California tax equal to their share of the tax paid by the business entity. The credit would be allowed to reduce regular tax below TMT and would be allowed after the other state tax credit.

Using available tax return data, an analysis was completed to identify taxpayers with business income to determine whether they would elect to pay the additional tax and how that election would impact California revenue.

This estimate analyzed the taxpayers' combined state and federal impact of electing to pay the additional tax. The estimate assumed that taxpayers would elect to pay the additional tax if the benefits from their federal tax savings from the reduction in pass-through income and credits generated with the state would be greater than the additional California tax paid. It is assumed this would result in a revenue gain to the state. For taxpayers whose combined state and federal benefits would result in a higher tax liability to the shareholder, it is assumed that they would not elect to pay the additional tax.

Applying the 9.3% tax rate to the qualified net income of qualified entities assumed to elect would produce a revenue gain of approximately $3,600,000,000 in tax year 2021 and $3,400,000,000 in tax year 2022. It is estimated that individual taxpayers will be able to use approximately $3,400,000,000 and $3,300,000,000 in tax credits in 2021 and 2022 respectively. The remaining credits may be used in the following five remaining years.

This results in net revenue gain of approximately $290,000,000 for tax year 2021 and $145,000,000 for tax year 2022.

The tax year estimates are then converted to fiscal year estimates, and then rounded to arrive at the amounts reflected in the above table.

LEGAL IMPACT

None noted.

Analysis Provision No. 2: Repeal of Business Tax Credit Limitation for 2022 (Sections 7, 16, and 25)

This provision would, under the PITL and CTL, repeal the business tax credit limitation, thereby removing the $5,000,000 credit cap for taxable years beginning on or after January 1, 2022.

For purposes of complying with RTC section 41, this provision, in Section 25 of the bill, does not contain additional information relating to the goals, purposes, and objectives of those tax expenditures for ending the temporary business tax credit limitation one year earlier than currently provided.

Effective/Operative Date

As a provision within this bill, providing for appropriations relating to the Budget Bill and identified as a bill relating to the budget in the Budget Bill, would be effective immediately upon enactment and the repeal of the business credit limitation would be specifically operative for taxable years beginning on or after January 1, 2022.

Federal/State Law

Federal Law

Current federal law does not specify a dollar limit on the total amount of all credits that can reduce the tax due.

State Law

For taxable years beginning on or after January 1, 2020, and before January 1, 2023, business tax credit usage under the PITL and CTL is limited to $5,000,000. For taxpayers included in a combined report, this determination is made at the group level.

For purposes of the PITL credit limitation, the $5,000,000 credit limit applies to business credits. The definition of business credits specifically excludes the Low-income Housing Credit, the credits relating to earned income, young child, household and dependent care, adoption costs, renters, personal exemption, joint custody head of household and for care of dependent parent, senior head of household, and excess contributions of unemployment compensation. Business credits, as limited, are required to be applied against the tax due before the excluded credits.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

AB 85 (Assembly Committee on Budget, Chapter 8, Statutes of 2020), among other things, limited the use of business tax credits to $5,000,000 for taxable years 2020, 2021, and 2022, and extended the credit carryover period for credits it disallowed.

PROGRAM BACKGROUND

None noted.

ECONOMIC IMPACT

Revenue Estimate

This provision would result in the following revenue impact:

Estimated Revenue Impact of SB 113 Provision No. 2 as Amended on February 2, 2022
Assumed Enactment Prior to April 1, 2022

($ in Millions)

Fiscal Year	Revenue
2021-2022	-$1,200
2022-2023	-$2,300
2023-2024	-$5.4

This analysis does not account for changes in employment, personal income, or gross state product that could result from this provision or for the net final payment method of accrual.

Revenue Discussion

Using the Personal Income Tax and Corporation Income Tax micro-simulation models, it was determined that the impact of repealing the $5,000,000 business tax credit use limitation for taxable year 2022 would result in an estimated $4,200,000,000 revenue loss in taxable year 2022.

The tax year estimates are then converted to fiscal year estimates, and then rounded to arrive at the amounts reflected in the above table.

LEGAL IMPACT

None noted.

Analysis Provision No. 3: PTEET Election and Credit Modifications (Sections 8, 14, 15, and 26)

For taxable years beginning on or after January 1, 2021, and before January 1, 2026, Sections 14 and 15 of this bill, relating to the SBRA, would modify the definition of "qualified net income" of the qualified entity to also include guaranteed payments, as defined by IRC section 707(c), that are subject to tax under the PITL for the taxable year of each qualified taxpayer.

In addition, the definition of a "qualified entity" that can elect to pay the elective tax would be modified to allow an entity's partners, shareholders, or members to also include partnerships.

For taxable years beginning on or after January 1, 2021, and before January 1, 2026, Section 8 of this bill, would modify the provisions of the PTEET credit under the PITL, by modifying the definition of "qualified amount" to also include an amount equal to 9.3% of the qualified taxpayer's guaranteed payments as defined by IRC section 707(c), subject to tax under the PITL, and subject to the election made by the qualified entity under the SBRA.

Furthermore, the definition of a "qualified taxpayer" that can claim the credit would be modified to include an LLC that is disregarded for federal tax purposes that meets both of the following:

- Is owned by an individual, fiduciary, estate, or trust that consented to have the sum of their guaranteed payments and pro rata share or distributive share of income, as applicable, subject to tax under the PITL, included in qualified net income of the electing qualified entity under the SBRA.
- Is a partner, shareholder, or member of an electing qualified entity.

For purposes of complying with Section 41, the goal of the tax expenditures relating to the provision is to provide tax relief to small businesses facing unprecedented economic hurdles due to COVID-19.

Effective/Operative Date

As a provision within a bill providing for appropriations relating to the Budget Bill, this provision would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2021, and before January 1, 2026.

Federal/State Law

Federal Law

Federal law, prior to 2018, allowed individuals to deduct certain expenses, such as medical expenses, charitable contributions, interest, and taxes, as itemized deductions. Certain other expenses for the production of income and certain employee business expenses were considered miscellaneous itemized deductions and only the portion that exceeded 2% of adjusted gross income could be deducted. Also, itemized deductions were further limited for high-income taxpayers.

Federal law, for taxable years beginning on or after January 1, 2018, under the Tax Cuts and Jobs Act, changed several itemized deductions, including:

- Suspending both the deduction for miscellaneous itemized deductions and the overall limitation on itemized deductions for high-income taxpayers for taxable years beginning after December 31, 2017, and before January 1, 2026.
- Limiting the total deduction for state and local income, sales, and property taxes to $10,000 ($5,000 if married filing separate). This is commonly referred to as the state and local taxes (SALT) deduction limitation.

The Internal Revenue Service (IRS) issued Notice 2020-75, dated November 9, 2020, which provides that the Department of Treasury and the IRS intend to issue regulations clarifying that tax payments made at the entity level would not be subject to the SALT deduction limitation applicable to partners and shareholders, who itemize deductions. Specifically, the announcement said the proposed regulations would:

> "…clarify that State and local income taxes imposed on and paid by a partnership or an S corporation on its income are allowed as a deduction by the partnership or S corporation in computing its non-separately stated taxable income or loss for the taxable year of payment, and therefore are not subject to the State and local tax deduction limitation for partners and shareholders who itemize deductions."

The Notice provides that these pass-through entities (PTEs) can pay SALT at the entity level, and the tax deduction that flows through to the individual partners and shareholders will not be subject to the individual SALT limitation for itemized deduction purposes.

In addition, existing federal laws provide various tax credits designed to provide tax relief for taxpayers who incur certain expenses (e.g., child adoption or first-time home buying) or to influence behavior, including business practices and decisions (e.g., research credits or hiring credits). These credits generally are designed to provide incentives for taxpayers to perform various actions or activities that they may not otherwise undertake.

There is no federal credit currently comparable to the California PTEET tax credit.

State Law

State law generally conforms to federal law as of the "specified date" of January 1, 2015, with modifications, allowing individuals to deduct certain expenses, such as medical expenses, charitable contributions, interest, and taxes, as itemized deductions. State law retains the deduction for SALT, miscellaneous itemized deductions, and the limitation on itemized deductions for high-income taxpayers.

Elective Tax at Entity Level

The SBRA, under Part 10.4 of the RTC, for taxable years beginning on or after January 1, 2021, and before January 1, 2026, allows a qualified entity doing business in this state to annually elect to pay an elective tax. For entities required to file a return under Sections 18633 (partnership returns), 18633.5 (LLC returns), or 18601 (S corporation returns), the elective tax is 9.3% of the qualified net income for the taxable year for which the election is made. The qualified net income of the qualified entity is the sum of the pro rata share or distributive share of income subject to tax under the PITL for the taxable year of each qualified taxpayer that consents.

For purposes of the SBRA, a qualified entity means an entity that is taxed as a partnership or an S corporation; and that entity's partners, members, or shareholders in that taxable year are exclusively corporations as defined under the CTL, or individuals, fiduciaries, estates, or trusts subject to tax under the PITL. A qualified entity cannot be a publicly traded partnership or an entity permitted or required to be included in a combined reporting group.

PTEET Credit

Existing state laws also provide various tax credits designed to provide tax relief for taxpayers who incur certain expenses or to influence behavior, including business practices and decisions.

Under the PITL, for taxable years beginning on or after January 1, 2021, and before January 1, 2026, a qualified taxpayer, who is a partner, shareholder, or member of a qualified entity under the SBRA that makes an annual election to pay the elective tax, is allowed a PTEET tax credit in an amount equal to the qualified amount.

For the PTE tax credit, the following definitions apply:

- Electing qualified entity means a qualified entity, as defined above that has elected to pay the elective tax under the SBRA.
- Qualified amount means an amount equal to 9.3% of the qualified taxpayer's pro rata or distributive share, as applicable, of qualified net income subject to the election made by an electing qualified entity under the SBRA.
- Qualified taxpayer means a taxpayer that is an individual, fiduciary, estate, or trust that is a partner, shareholder, or member of an electing qualified entity that consented to have their pro rata share or distributive share of income included in the qualified net income of the electing qualified entity; and does not include a business entity that is disregarded for federal tax purposes, or its partners or members.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

SB 104 (McGuire and Caballero, et al., 2021/2022), similar to AB 150 (Committee on Budget, Chapter 82, Statutes of 2021), would have added to the RTC, Part 10.4, to create the SBRA, and would, for taxable years beginning on or after January 1, 2021, and before January 1, 2026, have allowed entities taxed as a partnership or an S corporation to pay an additional elective tax, at the entity level. In addition, under the PITL, SB 104 would have allowed a qualified taxpayer a PTEET credit in an amount equal to 94.9% of the owner's pro rata or distributive share of the elective tax amount paid by the qualified entity under the SBRA. This bill was held in the Senate without further action; however, most provisions of the bill were incorporated into AB 150.

AB 150 (Committee on Budget, Chapter 82, Statutes of 2021), created the SBRA, and for taxable years beginning on or after January 1, 2021, and before January 1, 2026, allows entities taxed as a partnership or an S corporation to pay an additional elective tax at the entity level. In addition, under the PITL, AB 150 allows a qualified taxpayer, who is an owner of a qualified entity that makes an annual election to pay an additional elective tax authorized by the bill, a tax credit in an amount equal to 9.3% of the qualified taxpayer's pro rata or distributive share, as applicable, of the qualified net income subject to the election made by an electing qualified entity for taxable years beginning on or after January 1, 2021, and before January 1, 2026.

PROGRAM BACKGROUND

None noted.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue impact:

Estimated Revenue Impact of SB 113 Provision No. 3 as Amended on February 2, 2022
Assumed Enactment Prior to April 1, 2022

($ in Millions)

Fiscal Year	Revenue
2021-2022	$60
2022-2023	$60
2023-2024	$50

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

This provision would allow additional entities specified under the bill to elect to pay an additional tax of 9.3% on their business income and allow guaranteed tax payments to be treated as qualified income. This additional tax would reduce the amount of income the owners of those businesses would have to report for federal tax purposes. In addition, owners would receive a credit against California tax equal to their share of the tax paid by the business entity.

Using available tax return data, an analysis was completed to identify taxpayers with business income to determine whether they would elect to pay the additional tax and how that election would impact California revenue.

This estimate analyzed the taxpayers' combined state and federal impact of electing to pay the additional tax. The estimate assumed that taxpayers would elect to pay the additional tax if the benefits from their federal tax savings from the reduction in pass-through income and credits generated with the state would be greater than the additional California tax paid. It is assumed this would result in a revenue gain to the

state. For taxpayers whose combined state and federal benefits would result in a higher tax liability to the shareholder, it is assumed that they would not elect to pay the additional tax.

Applying the 9.3% tax rate to the qualified net income of qualified entities assumed to elect would produce a revenue gain of approximately $660,000,000 in tax year 2021 and $510,000,000 in tax year 2022. It is estimated that individual taxpayers will be able to use approximately $585,000,000 and $460,000,000 in tax credits in 2021 and 2022 respectively. The remaining credits may be used in the following five remaining years.

This results in net revenue gain of approximately $90,000,000 for tax year 2021 and $50,000,000 for tax year 2022.

The tax year estimates are then converted to fiscal year estimates, and then rounded to arrive at the amounts reflected in the above table.

LEGAL IMPACT

None noted.

Analysis Provision No. 4: Gross Income Exclusion of Water and Wastewater System Payments (Sections 9, 19, and 23)

This provision, under PITL and CTL, would, for taxable years beginning on or after January 1, 2021, and before January 1, 2026, exclude from gross income a bill credit or credits received by a customer from a community water system or wastewater treatment provider.

For purposes of complying with Section 41, these provisions state that the Legislature finds and declares that the specific goal, purpose, and objective for the gross income exclusion is to provide financial relief to California businesses and individuals who are impacted by the disruptions and hardships based on COVID-19 emergency.

For purposes of the exclusion related to assistance from a community water system or wastewater treatment provider, the State Water Resources Control Board (SWRCB) would be required to prepare a written report that includes the following, the total number of:

- Households that received water system bill credits.
- Commercial customers that received water system bill credits.
- Households that received wastewater system bill credits.
- Commercial customers that received wastewater system bill credits.

This provision would be repealed on December 1, 2026.

Effective/Operative Date

The gross income exclusion provision would be specifically operative, for taxable years beginning on or after January 1, 2021, and before January 1, 2026. The reporting requirements would be effective immediately upon enactment.

Federal/State Law

Federal Law

The American Rescue Plan Act (ARPA) (Public Law (PL) 117-2) allocated $500,000,000,000 in grants to states and Indian tribes to assist low-income households who pay higher proportions of household income for drinking water and wastewater services by providing funds to owners and operators of public water systems or treatment works to reduce arrearages and rates for these services.

Additionally, under the ARPA and the Consolidated Appropriations Act of 2021 (CAA) (PL 116-260), funds were appropriated to states for rental and homeowner's assistance to prevent homeowner and renter delinquencies, loss of utilities or home energy services, and displacements through qualified expenses related to mortgages and housing. The qualified expenses include assistance such as, renter and mortgage payment assistance, payment assistance for utilities (electric, gas, home energy, and water), and internet service.

Current federal law allows an exclusion from gross income any amounts received by an individual as a qualified disaster relief payment. A qualified disaster relief payment is any amount paid to or for the benefit of an individual if an amount is paid by federal, state, or local government in connection with a qualified disaster supporting the general public's welfare. A qualified disaster is defined as a disaster (such as the COVID-19 pandemic) determined by a federal, state, or local authority that warrants assistance from the federal, state, or local government or agency.

State Law

California generally conforms to IRC section 61 pursuant to RTC sections 17071 and 24271 as of January 1, 2015, except as otherwise provided. Additionally, California conforms by reference to Part III of Subchapter B of Chapter 1 of Subtitle A of the IRC, relating to items that are specifically excluded from gross income, as of January 1, 2015, in RTC section 17131. California will generally follow federal law for the treatment of qualified disaster payments.

For taxable years beginning on or after January 1, 2020, and before January 1, 2025, California law provides an exclusion from gross income for a tenant's rent liability that is forgiven by a landlord under the State Rental Assistance Program (SRAP) or as rent forgiveness provided through direct allocations of funding received by grantees under the CAA.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

AB 81 (Ting, Chapter 5, Statutes of 2021) made several clarifying amendments and technical changes to existing state law related to state assistance to individuals impacted by the COVID-19 pandemic, including the SRAP, which includes provisions exempting rent forgiveness and certain rental assistance payments from gross income for purposes of the PITL.

SB 91 (Senate Committee on Budget and Fiscal Review, Chapter 2, Statutes of 2021) provides a gross income exclusion for certain rental assistance received under the SRAP and the federal CAA.

PROGRAM BACKGROUND

The United States (U.S.) Department of Health and Human Services administers the Low Income Household Water Assistance Program (LIHWAP)(established under ARPA) and Low Income Home Energy Assistance Program (LIHEAP). LIHWAP grants are available to states who received LIHEAP grants to assist low income households with water, wastewater, and utility bills.

The Water and Wastewater Arrearage Payment Program was established within the SWRCB. The SWRCB works with community water systems and wastewater treatment providers to determine statewide arrearages and coordinate with Department of Community Services and Development (CSD) in allocating program funding to community water systems that are publicly owned utilities providing electric and water services.

ECONOMIC IMPACT

Revenue Estimate

SB 113 Provision No. 4 as amended February 2, 2022, would not impact state income or franchise tax revenue.

Revenue Discussion

IRC section 139 treats the water relief credits authorized under the ARPA as disaster relief payments excluded from gross income. California will generally follow federal law for the treatment of qualified disaster payments; therefore, there is no revenue impact.

LEGAL IMPACT

None noted.

Analysis Provision No. 5: Gross Income Exclusion of CAPP (Sections 10, 20, and 24)

This provision, under PITL and CTL, would, for taxable years beginning on or after January 1, 2021, and before January 1, 2026, exclude from gross income a bill credit or credits received by a customer from an energy utility applicant under the CAPP.

For purposes of complying with Section 41, these provisions state that the Legislature finds and declares that the specific goal, purpose, and objective for the gross income exclusion is to provide financial relief to California businesses and individuals who are impacted by the disruptions and hardships based on COVID-19 emergency. In addition, the CSD would be required to prepare a written report for the Legislature as required by the CAPP under the ARPA. (Government Code section 16429.5(j).)

This provision would be repealed on December 1, 2026.

Effective/Operative Date

The gross income exclusion provision would be specifically operative, for taxable years beginning on or after January 1, 2021, and before January 1, 2026. The reporting requirements would be effective immediately upon enactment.

Federal/State Law

Federal Law

Under ARPA and CAA, funds were appropriated to states for rental and homeowner's assistance to prevent homeowner and renter delinquencies, loss of utilities or home energy services, and displacements through qualified expenses related to mortgages and housing. The qualified expenses include assistance such as, renter and mortgage payment assistance, payment assistance for utilities (electric, gas, home energy, and water), and internet service.

Current federal law allows an exclusion from gross income any amounts received by an individual as a qualified disaster relief payment. A qualified disaster relief payment is any amount paid to or for the benefit of an individual if an amount is paid by federal, state, or local government in connection with a qualified disaster supporting the general public's welfare. A qualified disaster is defined as a disaster (such as the COVID-19 pandemic) determined by a federal, state, or local authority that warrants assistance from the federal, state, or local government or agency.

State Law

California generally conforms to IRC section 61 pursuant to RTC sections 17071 and 24271 as of January 1, 2015, except as otherwise provided. Additionally, California conforms by reference to Part III of Subchapter B of Chapter 1 of Subtitle A of the IRC, relating to items that are specifically excluded from gross income, as of January 1, 2015, in RTC section 17131. California will generally follow federal law for the treatment of qualified disaster payments.

For taxable years beginning on or after January 1, 2020, and before January 1, 2025, California law provides an exclusion from gross income for a tenant's rent liability that is forgiven by a landlord under the SRAP or as rent forgiveness provided through direct allocations of funding received by grantees under the CAA.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

AB 81 (Ting, Chapter 5, Statutes of 2021) made several clarifying amendments and technical changes to existing state law related to state assistance to individuals impacted by the COVID-19 pandemic, including the SRAP, which includes provisions exempting rent forgiveness and certain rental assistance payments from gross income for purposes of the PITL.

SB 91 (Senate Committee on Budget and Fiscal Review, Chapter 2, Statutes of 2021) provides a gross income exclusion for certain rental assistance received under the SRAP and the CAA.

PROGRAM BACKGROUND

The U.S. Department of Health and Human Services administers the LIHWAP (established under ARPA) and the LIHEAP. LIHWAP grants are available to states who received LIHEAP grants to assist low income households with water, wastewater, and utility bills.

CAPP was established within the CSD to distribute ARPA funding. CSD works with utility applicants to obtain the number of residential and commercial customer accounts in arrears and develop an allocation formula to determine a utility applicant's share of CAPP funds. The CAPP funds are available to utility applicants, which are defined as a local publicly owned electric utility, an electrical corporation or gas corporation utility, or an electrical cooperative.

ECONOMIC IMPACT

Revenue Estimate

SB 113 Provision No. 5 as amended February 2, 2022, would not impact state income or franchise tax revenue.

Revenue Discussion

IRC section 139 treats the utility relief credits authorized under the ARPA as disaster relief payments excluded from gross income. California will generally follow federal law for the treatment of qualified disaster payments; therefore, there is no revenue impact.

LEGAL IMPACT

None noted.

Analysis Provision No. 6: Gross Income Exclusion of RRG (Sections 11, 17, 22, and 27)

This provision, under the PITL and CTL, would exclude from gross income a grant amount awarded as a RRG under the ARPA for taxable years beginning on or after January 1, 2020.

In addition, this provision would adopt the provisions of the ARPA that prohibit any denial of tax deductions, denials of basis increases, and prevent required reductions in tax attributes based on the exclusion from gross income provided for any grant amount awarded.

The rulemaking procedures under the Administrative Procedure Act would not apply to any standard, criterion, procedure, determination, rule, notice, guideline, or any other guidance established or issued by the Franchise Tax Board (FTB) pursuant to this provision.

For purposes of complying with Section 41, this provision states that the Legislature finds and declares that the specific goal, purpose, and objective that the exclusions, deductions, tax basis, and other attributes will achieve is to provide relief to California restaurants that have been harmed economically by the COVID-19 pandemic.

The Legislative Analyst's Office (LAO) would be required to collaborate with the FTB, as well as reviewing other publicly available data, to analyze whether a RRG and related tax benefits for each were distributed evenly over the business community harmed by the COVID-19 pandemic. The LAO may request information from the FTB for purposes of this data collection requirement. The FTB would be required to provide any available data requested by the LAO pursuant to this subdivision and the required disclosure would be an exception to the general prohibition against disclosure of information filed with FTB. The report would be required to be provided to the Legislature by January 1, 2024.

This provision states that the Legislature's intent for authorizing the gross income exclusion and tax benefits under the RRG program secures the financial condition for California businesses that suffered from the COVID-19 pandemic and do not provide a gift of public funds.

Effective/Operative Date

As a provision within a bill providing for appropriations related to the Budget Bill, this provision would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2020.

Federal/State Law

Federal Law

ARPA establishes the Restaurant Revitalization Fund (RRF) and appropriates $28,600,000,000 for the Small Business Administration (SBA) to provide grants to an eligible entity. During the covered period, grants can be used for certain expenses incurred as a direct result of, or during, the COVID–19 pandemic. The specific expenses generally include payroll costs, principal or interest on mortgage payments, rent payments, utilities, maintenance expenses, supplies, food and beverage expenses, covered supplier costs, operational expenses, paid sick leave, and other expenses SBA determines to be essential to maintaining the eligible entity.

Eligible entities can receive a grant amount equal to their "pandemic-related revenue loss," which is defined as the eligible entity's gross receipts during 2020 minus their gross receipts during 2019, if the sum is more than $0. Different rules apply for eligible entities not in operation for all of 2019 that opened during 2020, or had incurred certain expenses but had not opened by the time of application. The aggregate grant amount cannot exceed $10,000,000 to an eligible entity and any affiliated businesses

of the eligible entity, and is limited to $5,000,000 per physical location of the eligible entity. Eligible entities that do not use all grant funds or permanently cease operations on or before the last day of the covered period will be required to return any funds not used for allowable expenses.

Under ARPA Section 9673, eligible entities can exclude from gross income received RRGs. Deductions are allowed for expenses paid and that tax basis and other tax attributes will not be modified as a result of the gross income exclusion. Additionally, certain tax basis adjustments related to partnerships and S corporation will be applied.

State Law

California generally conforms to IRC section 61 pursuant to RTC sections 17071 and 24271 as of January 1, 2015, except as otherwise provided. For taxable years beginning on or after January 1, 2019, California conforms to the exclusion from gross income for covered loan amounts that are forgiven under the Paycheck Protection Program (PPP) established by Section 1106 of the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) (HR748; PL 116-136), and modified by the Paycheck Protection Program and Health Care Enhancement Act, and Paycheck Program Flexibility Act of 2020.

California also conforms to the exclusion from gross income of PPP covered loan amounts, PPP Second Draw loans, and Economic Injury Disaster Loan (EIDL) advance grant amounts that are forgiven under the CAA for taxable years beginning on or after January 1, 2019.

California does not conform to the federal RRG program.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

AB 80 (Burke, Chapter 17, Statutes of 2021), for taxable years beginning on or after January 1, 2019, under the PITL and the CTL, expanded the exclusion from gross income for covered loan amounts forgiven pursuant to California conformity to certain federal provisions. This bill also conformed to the exclusion from gross income for

advance grant amounts forgiven pursuant to certain federal provisions, and conformed to the allowance of deductions and treatment of tax basis and other tax attributes relating to business expenses paid with forgiven covered loan amounts under the PPP, except for ineligible entities, as specified.

AB 1577 (Burke, Chapter 39, Statutes of 2020), under the PITL and the CTL, provided an exclusion from gross income covered loan amounts forgiven pursuant to the federal CARES Act, Paycheck Protection Program and Health Care Enhancement Act, or the Paycheck Program Flexibility Act of 2020 for taxable years beginning on and after January 1, 2020. It also prohibited the deduction of expenses paid with excluded income.

PROGRAM BACKGROUND

None noted.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of SB 113 Provision No. 6 as Amended on February 2, 2022
Assumed Enactment Prior to April 1, 2022

($ in Millions)

Fiscal Year	Revenue
2021-2022	-$110
2022-2023	-$120
2023-2024	-$95

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 data from the U.S. SBA’s RRF Program, California taxpayers received approximately $5,700,000,000 from all approved RRG funding.

Applying an average tax rate of 7% would result in an estimated total revenue loss of approximately $390,000,000. It is estimated the revenue impact would take place over a period of five years and that approximately 40%, or $160,000,000, would occur during the 2021 and 2022 taxable years.

The tax year estimates are then converted to fiscal year estimates and then rounded to arrive at the amounts reflected in the above table. Any revenue associated with a prior tax year are accrued back one year.

LEGAL IMPACT

None noted.

Analysis Provision No. 7: Gross Income Exclusion of SVOG (Sections 12, 18, 22, and 27)

This provision, under the PITL and CTL, would exclude from gross income a grant amount awarded as a "Shuttered Venue Operator Grant" under the CAA, for taxable years beginning on or after January 1, 2019.

In addition, this provision would adopt the provisions of the CAA that prohibit any denial of tax deductions, denials of basis increases, and prevent required reductions in tax attributes based on the exclusion from gross income provided for any grant amount, except for an ineligible entity, as defined.

For purposes of this provision:

"Ineligible entity" means a taxpayer that either:

a. Is a publicly-traded company.
b. Does not meet a 25% or more reduction in gross receipts in 2020 as compared to the same period in 2019 requirement for issuance of covered loans under the PPP, as added by the CAA. There are additional rules provided for new businesses.

For purposes of complying with Section 41, this provision states that the Legislature finds and declares that the specific goal, purpose, and objective that the exclusions, deductions, tax basis, and other attributes will achieve is to provide relief to California shuttered venue operators that have been harmed economically by the COVID-19 pandemic.

The LAO would be required to collaborate with the FTB, as well as reviewing other publicly available data, to analyze whether a SVOG and related tax benefits for each were distributed evenly over the business community harmed by the COVID-19 pandemic. The LAO may request information from the FTB for purposes of this data collection requirement. The FTB would be required to provide any available data requested by the LAO pursuant to this subdivision and the required disclosure would

be an exception to the general prohibition against disclosure of information filed with FTB. The report would be required to be provided to the Legislature by January 1, 2024.

This provision states that the Legislature's intent for authorizing the gross income exclusion and tax benefits under the SVOG program secures the financial condition for California businesses that suffered from the COVID-19 pandemic and do not provide a gift of public funds.

Effective/Operative Date

As a provision within a bill providing for appropriations related to the Budget Bill, this provision would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2019.

Federal/State Law

Federal Law

Section 324 of the Economic Aid to Hard-Hit Small Businesses, Nonprofits, and Venues Act (CAA, PL 116-260)(Title 15 U.S. Code section 9009a) establishes the grants for shuttered venue operators. An eligible person or entity that is a live venue operator or promoter, theatrical producer, or live performing arts organization operator, a motion picture theatre operator or a talent representative who has gross earned revenue during the first, second, third, or for an application submitted on or after January 1, 2021, fourth quarter in 2020 that demonstrates no less than a 25% reduction from the gross earned revenue during the same quarter in 2019 is eligible for a grant.

The grant amount is equal to 45% of their 2019 gross earned income or $10,000,000, whichever is less. For an operator who is in operation after January 1, 2019, the grant amount is the average monthly gross earned income for each month in operation during 2019 multiplied by six or $10,000,000, whichever is less. Grants must be used for certain expenses incurred, including payroll costs, scheduled mortgage payments, rent payments, covered utility payments, and Form-1099 MISC payments made to independent contractors beginning on March 1, 2020, and ending on June 30, 2022. Grants will not be provided to an eligible person or entity who is a publicly-traded company or who received more than 10% of gross revenue from federal funding in 2019.

Under CAA section 278, shuttered venue operators are eligible for an exclusion from gross income for grant amounts awarded, for taxable years ending after December 27, 2020. Additionally, no basis or tax attribute adjustment is required with respect to the exclusion from income of the forgiven debt.

ARPA extended the CAA funding for SVOG and requires the grant amount to be reduced by the amount of any received PPP covered loan.

State Law

California generally conforms to IRC section 61 pursuant to RTC sections 17071 and 24271 as of January 1, 2015, except as otherwise provided. For taxable years beginning on or after January 1, 2019, California conforms to the exclusion from gross income for covered loan amounts that are forgiven under the PPP established by Section 1106 of the CARES Act, and modified by the Paycheck Protection Program and Health Care Enhancement Act, and Paycheck Program Flexibility Act of 2020.

California also conforms to the exclusion from gross income of PPP covered loan amounts, PPP Second Draw loans, and EIDL advance grant amounts that are forgiven under the CAA for taxable years beginning on or after January 1, 2019.

California does not conform to the federal SVOG program.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

AB 80 (Burke, Chapter 17, Statutes of 2021), for taxable years beginning on or after January 1, 2019, under the PITL and the CTL, expanded the exclusion from gross income for covered loan amounts forgiven pursuant to California conformity to certain federal provisions. This bill also conformed to the exclusion from gross income for advance grant amounts forgiven pursuant to certain federal provisions, and conformed to the allowance of deductions and treatment of tax basis and other tax attributes relating to business expenses paid with forgiven covered loan amounts under the PPP, except for ineligible entities, as specified.

AB 1577 (Burke, Chapter 39, Statutes of 2020), under the PITL and the CTL, provided an exclusion from gross income covered loan amounts forgiven pursuant to the federal CARES Act, Paycheck Protection Program and Health Care Enhancement Act, or the Paycheck Program Flexibility Act of 2020 for taxable years beginning on and after January 1, 2020. It also prohibited the deduction of expenses paid with excluded income.

PROGRAM BACKGROUND

None noted.

ECONOMIC IMPACT

Revenue Estimate

This provision would result in the following revenue loss:

Estimated Revenue Impact of SB 113 Provision No. 7 as Amended on February 2, 2022
Assumed Enactment Prior to April 1, 2022

($ in Millions)

Fiscal Year	Revenue
2021-2022	-$47
2022-2023	-$50
2023-2024	-$41

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 data from the U.S. SBA's SVOG program, California taxpayers received approximately $2,500,000,000 from all approved SVOG funding.

Applying an average tax rate of 7% would result in an estimated total revenue loss of approximately $165,000,000. It is estimated the revenue impact would take place over a period of five years and that approximately 40% or $65,000,000, would occur during the 2021 and 2022 taxable years.

The tax year estimates are then converted to fiscal year estimates, and then rounded to arrive at the amounts reflected in the above table. Any revenue associated with a prior tax year are accrued back one year.

LEGAL IMPACT

None noted.

Analysis Provision No. 8: Repeal of NOL Deduction Suspension for 2022 (Sections 13, 21, and 25)

This provision would repeal the existing NOL deduction suspension, and therefore would allow NOL deductions for taxable years beginning on or after January 1, 2022.

For purposes of complying with RTC section 41, Section 25 of this bill indicates this provision ends the temporary limitation or suspension of existing tax expenditures one year earlier than currently provided and does not contain additional information related to the goals, purposes, and objectives of those tax expenditures.

Effective/Operative Date

As a provision within a bill providing for appropriations relating to the Budget Bill, this provision would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2022.

Federal/State Law

Federal Law

A NOL generally means the amount by which a taxpayer's business deductions exceed its gross income. The taxpayer generally may carry forward that NOL and deduct it in a subsequent taxable year.

Prior to the CARES Act

For NOLs arising in taxable years beginning after December 31, 2017, the NOL deduction generally is limited to 80% of taxable income determined without regard to the NOL deduction. Excess losses generally may be carried forward indefinitely, but not back, and carryovers of such NOLs to other taxable years are adjusted to take account of the 80% taxable income limitation. NOLs offset taxable income in the order of the taxable years to which the NOL may be carried.

NOLs arising in taxable years beginning before January 1, 2018, are not subject to the 80% taxable income limitation. Further, such NOLs remain subject to the 20-year carryover period and the relevant carryback rules in effect for taxable years beginning before January 1, 2018.

A taxpayer with NOL carryovers to a taxable year from both taxable years beginning before 2018 and taxable years beginning after 2017 computes its tax liability as follows. First, the taxpayer may deduct an NOL in the amount of its pre-2018 NOL carryovers without limitation. Second, the taxpayer may deduct an additional NOL equal to the lesser of (1) its post-2017 NOL carryovers or (2) 80% of the excess (if any) of the taxpayer's taxable income (before any NOL deduction attributable to post-2017 NOL carryovers) over the NOL deduction attributable to pre-2018 NOL carryovers.

Changes made by the CARES Act

The CARES Act suspended the application of the 80% taxable income limitation for taxable years beginning after December 31, 2017, and before January 1, 2021. The 80% taxable income limitation continues to apply in the case of any taxable year beginning after December 31, 2020. The 80% taxable income limitation was also eliminated for NOLs arising in taxable years beginning after December 31, 2017, that were generated in taxable years beginning on or before December 31, 2017, and carried to such a taxable year. (IRC section 172(a)(2). IRC section 172(a)(2)(A) provides that NOLs arising in taxable years beginning before January 1, 2018, carried to a taxable year beginning after December 31, 2020, are not subject to the 80% taxable income limitation.)

The CARES Act also modified the rules regarding carrybacks for NOLs arising in 2018, 2019, and 2020. Specifically, any NOL arising in a taxable year beginning after December 31, 2017, and before January 1, 2021, may be carried back to the five taxable years preceding the taxable year of such loss. (IRC sections 172(b)(1)(D) and 172(b)(1)(D)(i). Pursuant to IRC section 172(b)(2), any NOL carryback must be carried to the earliest taxable years to which such loss may be carried. NOLs eligible for the five-year carryback period include, for example, those arising with respect to farming losses, which would otherwise be subject to a two-year carryback period. See e.g., IRC section 172(b)(1)(B).)

State Law

Over the years, there have been several changes to the California NOL provisions. In general, California allows a taxpayer to calculate an NOL in accordance with federal rules, but has not conformed to the federal changes that apply to taxable years beginning after December 31, 2017.

NOLs attributable to taxable years beginning on or after January 1, 2008, may be carried forward 20 years. For NOLs attributable to taxable years beginning before January 1, 2013, and after December 31, 2018, NOL carrybacks are unavailable. California conforms to the federal NOL carryback rules for NOLs attributable to taxable years beginning on or after January 1, 2013, and before January 1, 2019, with modifications.

California law provides that losses generated in taxable years beginning on or after January 1, 2013, and before January 1, 2019, are allowed to be carried back to the two preceding taxable years.

The carryback was phased in as follows:

- 50% of the NOL generated in taxable years beginning in 2013 is eligible for a two-year carryback.
- 75% of the NOL generated in taxable years beginning in 2014 is eligible for a two-year carryback.
- 100% of the NOL generated in taxable years beginning in 2015 through 2018 is eligible for a two-year carryback.

For taxable years beginning in 2008 and 2009, California suspended the NOL carryover deduction. Taxpayers continued to compute and carryover their NOL during the suspension period. However, individuals with a net business income of less than $500,000, and corporations with taxable income of less than $500,000, were not affected by the NOL suspension rules.

For taxable years beginning in 2010 and 2011, California suspended the NOL carryover deduction. Taxpayers continued to compute and carryover NOLs during the suspension period. However, individuals with a modified adjusted gross income of less than $300,000, and corporations with net income less than $300,000, were not affected by the NOL suspension rules.

The carryover period for any NOL or NOL carryover, for which a deduction is disallowed because of the 2008-2011 suspension, is extended by:

- One year for losses incurred in taxable years beginning on or after January 1, 2010, and before January 1, 2011.
- Two years for losses incurred in taxable years beginning on or after January 1, 2009, and before January 1, 2010.
- Three years for losses incurred in taxable years beginning on or after January 1, 2008, and before January 1, 2009.
- Four years for losses incurred in taxable years beginning before January 1, 2008.

For taxable years 2020, 2021, and 2022, California again suspended the NOL carryover deduction. The suspension of NOLs does not apply to a taxpayer:

- Under the PITL with modified adjusted gross income or net business income of less than $1,000,000. "Modified adjusted gross income" means the amount required to be shown as adjusted gross income on the federal tax return for the same taxable year without taking into consideration the NOL deduction. "Business income" means income from a trade or business, whether conducted by the taxpayer or by a pass-through entity (partnership or S corporation), income from rental activity, and income attributable to a farming business.

The NOL carryover period was extended by one year for NOLs incurred in taxable year 2021, two years for NOLs incurred in taxable year 2020, and three years for NOLs incurred in taxable years beginning before 2020.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

AB 222 (Rubio, 2021/2022), under PITL and CTL, would have allowed certain qualified taxpayers to carryback suspended NOLs or suspended NOL carryovers in taxable years beginning on or after January 1, 2023, to each of the three preceding taxable years. AB 222 did not pass out of the Assembly by the constitutional deadline.

AB 85 (Committee on Budget, Chapter 8, Statutes of 2020), a budget trailer bill, amongst other provisions, suspended the use of NOL deductions. The suspension does not apply to taxpayers with modified adjusted gross income of less than $1,000,000 under the PITL or for taxpayers with net business income subject to tax under the CTL of less than $1,000,000 for taxable years 2020, 2021, and 2022. It also extended the carryover period for NOL deductions disallowed under this suspension.

AB 91 (Burke, Chapter 39, Statutes of 2019) disallowed the carryback of NOLs that were incurred in taxable years beginning on or after January 1, 2019, for individual and corporate taxpayers.

AB 154 (Ting, Chapter 359, Statutes of 2015) conformed to the federal NOL rules that allow corporations expecting an NOL carryback to extend the time for payment of taxes for the preceding taxable year.

AB 2166 (Kiley, 2019/2020), under PITL and CTL, would have conformed to federal law by allowing a five-year carryback of an NOL incurred in a taxable year that began on or after January 1, 2018, and before January 1, 2021, and by allowing an election to file a short period return for the first six months of a taxable year in which such an NOL was incurred. This bill did not pass out of the Assembly Revenue and Taxation Committee by the constitutional deadline.

AB 2855 (Brough, 2017/2018) would have established an application for a tentative refund process, similar to the federal process for obtaining a tentative refund based on an NOL carryback, and specified the trigger date for the statute of limitations and interest accrual applicable to an NOL carryback. AB 2855 did not pass out of the Senate Appropriations Committee by the constitutional deadline.

PROGRAM BACKGROUND

None noted.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue impact:

Estimated Revenue Impact of SB 113 Provision No. 8 as Amended on February 2, 2022
Assumed Enactment Prior to April 1, 2022

($ in Millions)

Fiscal Year	Revenue
2021-2022	-$800
2022-2023	-$1,300
2023-2024	$170

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 Personal Income Tax and Corporation Income Tax micro-simulation models, it was determined that the impact of repealing the NOL deduction suspension for taxable year 2022 would result is an estimated $2,600,000,000 revenue loss in taxable year 2022. The revenue estimate for this provision also considers the impact of the interaction between this provision and Provision No. 2, the repeal of business tax credit limitation for 2022.

The tax year estimates are then converted to fiscal year estimates, and then rounded to arrive at the amounts reflected in the above table.

LEGAL IMPACT

None noted.

APPOINTMENTS (All Provisions)

None noted.

SUPPORT/OPPOSITION (All Provisions)

None noted.

ARGUMENTS (All Provisions)

None noted.

LEGISLATIVE CONTACT

FTBLegislativeServices@ftb.ca.gov