STATE OF CALIFORNIA
Franchise Tax Board

Bill Analysis

Author: Wiener	Sponsor:	Bill Number: SB 1336
	Related Bills: See Legislative History	Amended: April 28, 2022, and May 9, 2022

SUBJECT

Qualified Tax Expenditure Credit for Cannabis Businesses

SUMMARY

Under the Personal Income Tax Law (PITL) and Corporation Tax Law (CTL), this bill would, for taxable years beginning on or after January 1, 2023, and before January 1, 2028, allow a credit to a qualified taxpayer equal to 25 percent of the amount of the qualified taxpayer's qualified expenditures in the taxable year limited to $250,000.

RECOMMENDATION

No position.

SUMMARY OF AMENDMENTS

The April 28, 2022, amendments modified provisions of the PITL and CTL by adding a sunset date, indicating a maximum amount of credit, clarified the maximum credit amount for qualified taxpayers included in a combined report, and modified a definition.

The May 9, 2022, amendments defined terms, added limitations to a term, which was previously omitted under the CTL, limited the carryover period to 8 years, and included language to prevent multiple tax benefits.

The April 28, 2022 and May 9, 2022, amendments resolved all prior Implementation Considerations, all Technical Consideration and three Policy Considerations identified in the department analysis of the bill as amended on March 16, 2022. Two new Technical Considerations and one new Implementation Consideration were identified and one Policy Consideration remains.

REASON FOR THE BILL

The reason for this bill is to provide tax relief to licensed cannabis businesses for qualified expenditures.

ANALYSIS

This bill would, under the PITL and CTL, for taxable years beginning on or after January 1, 2023, and before January 1, 2028, allow a credit to a qualified taxpayer equal to 25 percent of the qualified taxpayer's qualified expenditures in the taxable year, not to exceed $250,000.

The taxable year maximum of $250,000 would apply to the aggregate gross receipts of all taxpayers that are required to or are authorized to be included in a combined report under Revenue and Taxation Code (RTC) section 25101 and RTC section 25101.15.

The bill defines the following terms:

"Qualified expenditures" means amounts paid or incurred by a qualified taxpayer for any of the following:

- Employment compensation for the employees of the qualified taxpayer. For the purposes of this bill, "employment compensation" means wages paid to full-time employees who are paid no less than 150 percent but no more than 350 percent of the applicable minimum wage. "Employment compensation" may include the monetary value to the full-time employee of health insurance benefits, childcare benefits, retirement benefits, or pension benefits.
- Safety-related equipment, training, and services. For purposes of this bill, "safety-related equipment, training, and services," means:
  - Equipment primarily used by employees of cannabis licensees to ensure their personal and occupational safety or the safety of customers of the cannabis licensees;
  - Training for nonmanagement employees on workplace hazards, including but not limited to, the Cal/OSHA (Division of Occupational Safety and Health) 30-hour training general industry outreach course as defined in Business and Professions Code (BPC) section 26051.5(a)(11)(A), and;
  - Services including, but not limited to, safety audits, security guards, security cameras, and fire risk mitigation.
- Workforce development for employees of the qualified taxpayer. For purposes of this bill, "workforce development" includes, but is not limited to, joint labor management training programs, membership in a joint apprenticeship training committee registered by the Division of Apprenticeship Standards, and a state-recognized high road training partnership, which is an initiative or project that models strategies for developing industry-based, worker-focused training partnerships, including labor-management partnerships.

“Qualified taxpayer” means a commercial cannabis business, licensed pursuant to Division 10 (commencing with Section 26000) of the BPC, related to cannabis.

“Full-time employee” means an individual who is either of the following:

- Paid wages by the qualified taxpayer for services not less than an average of 35 hours per week.
- A salaried employee who was paid compensation during the taxable year for full-time employment, as described in Section 515 of the Labor Code (LAB), which defines “full-time employment,” as employment in which an employee is employed for 40 hours per week.

“Minimum wage” means the wage established pursuant to Chapter 1 of Part 4 of Division 2 of the LAB, related to minimum wages as specified by type of work and condition.

This bill specifies that any deduction or credit otherwise allowed for any qualified expenditure made by the qualified taxpayer as a trade or business expense to an eligible individual must be reduced by the amount of this credit.

Unused credits may be carried over for eight years until the credit is exhausted.

This bill states the Legislature's intent to comply with the reporting requirements of RTC section 41.

The bill would remain in effect only until December 1, 2028, and as of that date would be repealed.

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, 2023, and before January 1, 2028.

Federal/State Law

Federal law states that no deduction or credit is allowed for any amount paid or incurred during the taxable year in carrying on any trade or business that consists of trafficking in specified controlled substances, including cannabis.

Existing state and federal laws provide various tax credits designed to provide tax relief for taxpayers who incur certain expenses (e.g., child adoption) 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.

Under the PITL, for taxable years beginning on or after January 1, 2020, and before January 1, 2025, licensees engaged in commercial cannabis activity, as defined in the BPC, may deduct expenses and claim tax credits, related to that trade or business.

Under the CTL, a licensee engaged in commercial cannabis activity is allowed deductions or credits that are otherwise allowable, assuming the entity has adequate records to substantiate these items.

Under RTC section 41, legislation that would create a new tax expenditure, which includes a credit, deduction, exclusion, exemption, or any other tax benefit as provided for by the state, is required to include specific goals, purposes, objectives, and performance measures to allow the Legislature to evaluate the effectiveness of the tax benefit.

Implementation Considerations

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

This bill uses the undefined term, "joint labor management training programs." The absence of definitions to clarify this term could lead to disputes with taxpayers. For clarity, it is recommended that the bill be amended.

Technical Considerations

This bill uses the term "aggregate gross receipts" when applying the credit limitation to all members of a combined report. It is recommended that subdivision (a)(2)(B) be modified as follows:

> Notwithstanding any provision of this part or Part 10.2 (commencing with Section 18401) to the contrary, for qualified taxpayers that are required to be included in a combined report under Section 25101 or 25110 or authorized to be included in a combined report under Section 25101.15, the limit specified in subparagraph (A) shall not reduce the aggregate amount of "tax," as defined in Section 23036, of all members of the combined report by more than two hundred fifty thousand dollars ($250,000).

In Sections 17053.64(d) and 23664(d) the phrase to "as a trade or business expense to an eligible individual" should be removed to in order to avoid a double benefit with respect to the same expenses.

Policy Considerations

This bill does not have Section 41 requirements specified, which are generally provided to allow periodic review of the effectiveness of income tax law changes by the Legislature.

LEGISLATIVE HISTORY

SB 603 (Bradford, 2021/2022), would under the PITL and CTL, create a Cannabis Equity Business Tax Credit, related to licensing fees for certain cannabis businesses. SB 603 is currently in the Assembly Revenue and Taxation Committee and Assembly Business and Professions Committee.

SB 1293 (Bradford, 2021/2022), would under the PITL and CTL, for taxable years beginning on or after January 1, 2022, and before January 1, 2027, allow a credit against the net tax to a qualified taxpayer for business expenses of the taxpayers trade or business that the taxpayer could not deduct or claim for that taxable year under the federal income tax laws. SB 1293 is currently in the Senate.

AB 37 (Jones-Sawyer, Chapter 792, Statutes of 2019) under the PITL, for taxable years beginning on or after January 1, 2020, and before January 1, 2025, allows licensees engaged in commercial cannabis activity, to deduct expenses and claim tax credits, related to that trade or business.

PROGRAM BACKGROUND

None noted.

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 SB1336 as Amended on May 9, 2022
Assumed Enactment after June 30, 2022

($ in Millions)

Fiscal Year	Revenue
2022-2023	-$100
2023-2024	-$310
2024-2025	-$440

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

The May 23, 2022, Senate Floor analysis listed the following support and opposition.

Support

United Food and Commercial Workers, Western States Council (sponsor), California Teamsters Public Affairs Council, Cannacraft, Eaze Technologies, INC., Embarc. Long Beach Green Room, March and Ash, MWG Holdings Group, Inc., Shryne Group, Inc., The Parent Company, UDW/AFSCME Local 3930.

Opposition

None received.

ARGUMENTS

Proponents

The author submitted the following statement in support, which reads:

Senate Bill 1336 provides targeted tax relief to responsible commercial cannabis employers by establishing a carryforward cannabis tax credit that is 25 percent of the following qualified business expenditures paid for or incurred in a taxable year:

- Employment compensation, that is equal to or above 150 percent of minimum wage including benefits, for the employees of the business.
- Safety-related equipment and services.
- Workforce development and safety training for employees

In the case where the credit allowed exceeds the net tax, under SB 1336 the excess may be carried over to reduce the net tax in the following taxable year, and succeeding years if necessary, until the credit is exhausted. The credit amount cannot exceed $250,000 and can only be taken against applicable taxes until 2028. California's legal cannabis industry currently faces an existential crisis as the state continues to battle a thriving illicit market. Roughly $8 billion in sales flow through California's illicit cannabis market each year, which is about double the amount of legal sales – and some estimates are even larger. A thriving illicit market is having, and will continue to have, significant impacts on workers in the cannabis industry. If this trend continues, employers may be unable to maintain high worker wages, benefits, and career growth opportunities. In addition to the problems associated with their ineligibility for typical business relief, cannabis businesses also have additional overhead costs associated with health, safety, and security protections. Other businesses in California do not face these unique challenges. Targeted tax relief is needed to support California's struggling, legal cannabis businesses, and SB 1336 will provide this help.

Opposition

None received.

LEGISLATIVE CONTACT

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