STATE OF CALIFORNIA
Franchise Tax Board

Bill Analysis

Author: Senate Committee on Budget and Fiscal Review	Sponsor:	Bill Number: SB 167
	Related Bills: See Legislative History	Amended: June 10, 2024

SUBJECT

Budget Trailer Bill: Taxation Provisions

SUMMARY

This bill would do the following:

Provision No. 1 - $5 Million Credit Limitation:

Sections 15 and 33 of this bill would, under the Personal Income Tax Law (PITL) and Corporation Tax Law (CTL), for taxable years beginning on or after January 1, 2024, and before January 1, 2027, limit the total allowable tax reduction by all business credits to $5 million per taxable year. This provision would also extend the credit carryover period by the number of taxable years the credit was not allowed.

Provision No. 2 - California Earned Income Tax Credit (CalEITC), Young Child Tax Credit (YCTC), and Foster Youth tax Credit (FYTC) Aligned Maximum Income Threshold:

Sections 16 and 17 of this bill would, under the PITL, align the maximum income thresholds of the YCTC and FYTC with the CalEITC for taxable years beginning on or after January 1, 2024.

Provision No. 3 - Repeal of Enhanced Oil Recovery Costs Credit:

Sections 18 and 34 of this bill would, under the PITL and CTL, repeal the enhanced oil recovery credit for taxable years beginning on or after January 1, 2024.

Provision No. 4 - Extend Personal Income Tax Deduction and Credits Related to Commercial Cannabis Activities:

Section 19 of this bill would, under the PITL, extend the operation of the current provision which allows licensees engaged in commercial cannabis activity, to deduct expenses and claim tax credits, related to that trade or business until taxable years beginning on or after January 1, 2030.

Provision No. 5 - Eliminate the Deduction for Intangible Drilling and Development Costs:

Sections 20 and 37 of this bill would, under the PITL and CTL, eliminate the deduction for intangible drilling and development costs for oil and gas wells, for amounts paid or incurred on or after January 1, 2024.

Provision No. 6 - Conformity to Provisions Related to Charitable Deductions for Qualified Conservation Easement Contributions:

Sections 21, 22, 29, 30, and 35 would, under the PITL, the CTL and the Administration of Franchise and Income Tax Law (AFITL), conform, with modifications, to the federal charitable contribution deduction rules for qualified conservation easement contributions made by partnerships and other pass-through entities, for contributions made on or after January 1, 2024, and would also impose an Accuracy Related Penalty (ARP) and for disallowed deductions, would apply the same statute of limitations as applies under California law for abusive tax avoidance transactions.

Provision No. 7 – Net Operating Loss (NOL) Suspension:

Sections 23 and 36 of this bill would, under the PITL and CTL, disallow an NOL deduction for taxable years beginning on or after January 1, 2024, and before January 1, 2027, subject to certain income exceptions, and extend the NOL carryover period for NOL deductions disallowed under this provision.

Provision No. 8 - Repeal of the Percentage Depletion Method for Oil and Gas Well Producers:

Sections 24, 25, 26, 38, 39 and 40 of this bill would, under the PITL and CTL, repeal the percentage depletion method for oil shale, coal, and oil and gas well producers for taxable years beginning on or after January 1, 2024; and would make other technical corrections.

Provision No. 9 - Extension of Electronic Communications:

Section 27 of this bill would eliminate the repeal date for the Franchise Tax Board's (FTB's) authorization to, at the request of the taxpayer, send notifications electronically.

Provision No. 10 - State of Emergency Declarations:

Section 28 of this bill would, under the AFITL, authorize the Director of the Department of Finance (Director of Finance) to determine whether a taxpayer is affected by a state of emergency and whether tax deadlines should be postponed due to a state of emergency or a federally declared disaster.

Provision No. 11 - Terminate the Delinquent Tax Collection Fund:

Section 31 of this bill would, under the AFITL, repeal the Delinquent Tax Collection Fund upon the enactment of this bill.

Provision No. 12 - Extend the Strategic Aircraft Credit's Ability to Reduce Tax Below Tentative Minimum Tax (TMT):

Section 32 of this bill would, under the CTL, extend the taxpayer's ability to reduce tax below the TMT by the Strategic Aircraft Credit for five years from taxable years beginning before January 1, 2026, to taxable years beginning before January 1, 2031.

Provision No. 13 - Apportionment Formula:

Section 41 of this bill would, under the CTL, exclude a transaction or activity from the apportionment formula to the extent that it generates income or loss not included in net income. The provision also finds that it is the intent of the Legislature that the FTB Legal Ruling 2006-1, issued on April 28, 2006, would apply with respect to the apportionment formula of taxpayers subject to CTL. In addition, this provision would not constitute a change in but would be declaratory of existing law.

Provision No. 14 - Middle Class Tax Refund (MCTR) Clarification:

Section 43 of this bill would, under the Welfare and Institution Code (WIC), would clarify that any unexpended or unclaimed balance of MCTR payments, be returned to the FTB, which will deposit the moneys in the General Fund.

Annual Refundable Credit Election:

Section 45 of this bill would provide that it is the intent of the Legislature to allow taxpayers subject to the temporary credit limitation under Sections 15 and 33 of this bill the option to elect to receive a refund of those limited tax credits, as specified, and that the refundable credit amount can be adjusted by the FTB if the amount is determined to be overstated. See the analysis of SB 175 (Senate Committee on Budget and Fiscal Review, Chapter 42, Statutes of 2024), which contains the provisions of this optional election.

RECOMMENDATION

No position—The three-member FTB has not formally voted or taken a position on this bill.

SUMMARY OF AMENDMENTS

The June 10, 2024, amendments removed intent language relating to the Budget Act of 2024 and replaced it with the provisions discussed in this analysis.

This is the FTB's first analysis of the bill and only addresses the provisions that would impact the FTB.

REASON FOR THE BILL

The reason for the bill is to make various statutory changes relating to implementation of the Budget Act of 2024.

ANALYSIS

Analysis Provision No. 1:

$5 Million Credit Limitation (Sections 15 and 33 of this Bill)

This provision would make the following changes under the PITL and CTL:

- Limit the amount of business credits, as specified, to $5 million for taxable years beginning on or after January 1, 2024, and before January 1, 2027.
- Exclude various credits from the credit limitation.
- Increase the carryforward period for credits subject to the limitation by the number of taxable years the credit was not allowed.
- Specify that election under Revenue and Taxation Code (RTC) section 6902.5 to apply film credits against the sales and use tax would not be subject to this provision's credit limitation.
- Exempts any standard, criterion, procedure, determination, rule, notice, or guideline established or issued by the FTB pursuant to this provision from the requirements of the Administrative Procedure Act (APA).

For purposes of the PITL credit limitation, the $5 million credit limit would apply to "business credits," which would specifically exclude the credits relating to earned income, young child, foster youth, household and dependent care, elective tax under the Small Business Relief Act, adoption costs, renters, personal exemption, joint custody head of household and for care of dependent parent, senior head of household, excess contributions of unemployment compensation, and the Low Income Housing Credit (LIHC). Business credits, as limited, would be required to be applied against the tax due before the credits excluded from the definition of business credits. For purposes of the CTL credit limitation, the $5 million credit limit would apply to all credits, except for the LIHC.

Effective/Operative Date

This provision, as part of a bill providing for appropriation related to the Budget Bill, would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2024, and before January 1, 2027.

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, 2022, business credit usage under the PITL and CTL was limited to $5 million, similar to the limit this provision would impose.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

SB 113 (Senate Committee on Budget and Fiscal Review, Chapter 3, Statutes of 2022), under the PITL and CTL, amongst other provisions, repealed the business credit limitation for taxable years beginning on or after January 1, 2022, and before January 1, 2023.

AB 85 (Assembly Committee on Budget, Chapter 8, Statutes of 2020), under the PITL and CTL, among other provisions, limited the use of business tax credits to $5 million for taxable years beginning on or after January 1, 2020, and before January 1, 2023, and extended the credit carryover period for credits it disallowed.

PROGRAM BACKGROUND

None noted.

OTHER STATES' INFORMATION

None noted.

FISCAL IMPACT

The FTB anticipates minimal costs to implement this provision.

ECONOMIC IMPACT

Revenue Estimate

This provision would result in a revenue impact. In accordance with the bill provisions, staff defers to the Department of Finance (DOF) to determine the revenue impact of this provision.t

LEGAL IMPACT

None noted.

EQUITY IMPACT

None noted.

Analysis Provision No. 2:

CalEITC, YCTC, and FYTC Aligned Maximum Income Threshold (Sections 16 and 17 of this bill)

This provision would, under the PITL, for taxable years beginning on or after January 1, 2024, align the maximum income thresholds of the YCTC and FYTC with the CalEITC. The FTB would be required to calculate the graduated reduction amount in such a manner that would result in the YCTC and FYTC earned income phase out amounts to match the earned income phase out amount of the CalEITC.

Effective/Operative Date

This provision, as part of a bill providing for an appropriation relating to the Budget Bill, would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2024.

Federal/State Law

Earned Income Tax Credit

Existing federal law allows eligible individuals a refundable Earned Income Tax Credit (EITC) under Internal Revenue Code (IRC) section 32. The refundable credit allows for the excess of the credit over the taxpayer's tax liability to be refunded to the taxpayer. The EITC is a percentage of the taxpayer's earned income and is phased out as income increases. For 2023, the EITC is available to individuals and families earning up to $63,398.

State law provides a refundable CalEITC that is generally patterned after IRC section 32, as applicable for state income tax purposes for the taxable year, except as modified. For 2023, the CalEITC is generally available to taxpayers with earned income of $30,950 or less.

YCTC

Starting in 2019, a taxpayer who has been allowed the CalEITC and who has a qualifying child younger than six years old as of the last day of the taxable year may qualify for the YCTC. The maximum credit is limited to $1,000 per taxable year. The credit amount is reduced by $20 for every $100 by which the qualified taxpayer's earned income exceeds the threshold amount, initially set at $25,000. For taxable years after the minimum wage as defined by Section 1182.12 of the Labor Code is set at $15 per hour, the threshold amount will be recomputed annually in the same manner as the income tax brackets. For taxable year 2023, the YCTC is generally available to taxpayers with earned income of $30,931 or less.

FYTC

Starting in taxable year 2022, state law allows qualified taxpayers a refundable FYTC up to $1,083 per eligible individual or up to $2,166, if both primary taxpayer and spouse/registered domestic partner qualify. A qualified taxpayer is an individual allowed a CalEITC who is 18 to 25 years of age and was in foster care while 13 years of age or older in an Aid to Families with Dependent Children-Foster Care (AFDC-FC) placement, including a tribally approved home, or Approved Relative Caregiver Funding Program eligible placement, by a Title IV-E agency, pursuant to a voluntary placement agreement or a juvenile court order. The credit amount is equal to $1,083 multiplied by the EITC adjustment factor for the taxable year.

The FYTC is indexed for inflation and the credit amount is reduced by $20 for every $100 by which the qualified taxpayer's earned income exceeds the threshold amount of $25,000. The threshold amount and the $20 phaseout amount are also indexed for inflation. For taxable year 2023, the maximum FYTC amount of $1,117 and is generally available to taxpayers with earned income of $30,931 or less.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

AB 1498 (Gipson, 2023/2024) would have, under the PITL, established a minimum CalEITC, subject to appropriation, provided for the indexing of the minimum credit amount, and provided for a phaseout of the minimum credit amount among other provisions. AB 1498 did not pass out of the Assembly by the constitutional deadline.

SB 201 (Committee on Budget, Chapter 72, Statutes of 2022) Section 2 of the bill, among other provisions, under the PITL, for taxable years beginning on or after January 1, 2022, modified the YCTC to expand the definition of a qualified taxpayer, provided for indexing of the YCTC, enacted the FYTC, and made other technical nonsubstantive changes.

PROGRAM BACKGROUND

None noted.

OTHER STATES' INFORMATION

None noted.

FISCAL IMPACT

The FTB anticipates minimal costs to implement this provision.

ECONOMIC IMPACT

Revenue Estimate

This provision would result in a revenue impact. In accordance with the bill provisions, staff defers to the DOF to determine the revenue impact of this provision.

LEGAL IMPACT

None noted.

EQUITY IMPACT

None noted.

Analysis Provision No. 3:

Repeal of Enhanced Oil Recovery Costs Credit (Sections 18 and 34 of this Bill)

This provision would, under the PITL and CTL, make the enhanced oil recovery credit inoperative for taxable years beginning on or after January 1, 2024, and would repeal the credit on December 1, 2024.

Effective/Operative Date

This provision, as part of a bill providing for appropriation related to the Budget Bill, would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2024.

Federal/State Law

Federal Law

Existing federal law provides an enhanced oil recovery credit for any taxable year in an amount equal to 15% of the taxpayer's "qualified enhanced oil recovery costs" for such taxable year.

"Qualified Enhanced Oil Recovery Costs" means any of the following:

- Any amount paid or incurred during the taxable year for tangible property that–
    - Is an integral part of a qualified enhanced oil recovery project, and
    - Can be depreciated or amortized.

- Any intangible drilling and development costs that –
    - Are paid or incurred in connection with a qualified enhanced oil recovery project, and
    - The taxpayer may make an election under IRC section 263(c) for the taxable year.
- Any qualified tertiary injectant expenses (as defined in IRC section 193(b)) that are paid or incurred in connection with a qualified enhanced oil recovery project and for which a deduction is allowable for the taxable year.
- Any amount that is paid or incurred during the taxable year to construct specified gas treatment plants.

"Qualified enhanced oil recovery project" means any project —

- That involves the application of one or more tertiary recovery methods, which can reasonably be expected to result in more than an insignificant increase in the amount of crude oil which will ultimately be recovered;
- That is located within the United States; and
- With respect to which the first injection of liquids, gases, or other matter, that commences after December 31, 1990.

Phase-Out of Credit

The amount of credit is reduced (i.e. phased-out) by a ratio of the amount of the "reference price" that exceeds $28 adjusted every year by an inflation adjustment factor divided by $6.

The "reference price" is the annual average wellhead price for a barrel of oil for the last calendar year that ended before the taxable year in question.

Due to the generally high price of crude oil, the credit is usually completely phased-out, as seen in 2022 and 2023.

State Law

The California credit is generally the same as the federal credit except for the following:

- The California credit is one-third of the federal credit.
- The qualified enhanced oil recovery project must be located in California.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

ABX3-30 (Calderon, 2007/2008), identical to this provision, would have repealed the enhanced oil recovery credit for taxable years beginning on or after January 1, 2008. ABX3-30 did not pass out of the Assembly by the constitutional deadline.

PROGRAM BACKGROUND

None noted.

OTHER STATES' INFORMATION

None noted.

FISCAL IMPACT

The FTB anticipates minimal costs to implement this provision.

ECONOMIC IMPACT

Revenue Estimate

In accordance with the bill provisions, staff defers to the DOF to determine the revenue impact of this provision.

LEGAL IMPACT

None noted.

EQUITY IMPACT

None noted.

Analysis Provision No. 4:

Extend Personal Income Tax Deduction and Credits Related to Commercial Cannabis Activities (Section 19 of this Bill)

This provision would, under the PITL, extend the operation of the current provisions, which allows licensees engaged in commercial cannabis activity, to deduct expenses and claim tax credits, related to that trade or business, for an additional five years from taxable years beginning before January 1, 2025, to taxable years beginning before January 1, 2030.

This provision would be repealed on December 1, 2030.

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 operative for taxable years beginning on or after January 1, 2025, and before January 1, 2030.

Federal/State Law

Federal Law

Federal law provides that no deduction or credit is allowed for any amount paid or incurred for carrying on any trade or business that consists of trafficking in specified controlled substances, including cannabis. However, cannabis business owners are entitled to deduct their cost of goods sold from their gross receipts.

State Law

State law generally allows deductions and credits to cannabis businesses under PITL and CTL.

Under the PITL, for taxable years beginning on or after January 1, 2020, and before January 1, 2025, a licensee engaged in commercial cannabis activity is generally allowed to deduct expenses and claim tax credits related to that trade or business that are otherwise available to other businesses.

Under the CTL, a licensee engaged in commercial cannabis activity is generally allowed to deduct expenses and claim tax credits related to that trade or business that are otherwise available to other businesses.

In addition to the credits otherwise available to businesses, under the PITL and CTL, for taxable years beginning on or after January 1, 2023, and before January 1, 2028, licensed commercial cannabis businesses that meet specified requirements are allowed to claim the high-road cannabis tax credit and the cannabis equity tax credit.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

AB 37 (Jones-Sawyer, Chapter 792, Statutes of 2019) under the PITL, specified that the federal disallowance of deductions or credits related to the illegal sale of drugs would not apply to licensees engaged in the trade or business of commercial cannabis activities in the State.

PROGRAM BACKGROUND

None noted.

OTHER STATES' INFORMATION

None noted.

FISCAL IMPACT

The FTB anticipates minimal costs to implement this provision.

ECONOMIC IMPACT

Revenue Estimate

In accordance with the bill provisions, staff defers to the DOF to determine the revenue impact of this bill.

LEGAL IMPACT

None noted.

EQUITY IMPACT

None noted.

Analysis Provision No. 5:

Analysis Provision No. 5: Eliminate the Deduction for Intangible Drilling and Development Costs (Sections 20 and 37 of this bill)

The provision of this bill would, under the PITL and CTL, eliminate the deduction for intangible drilling and development costs for oil and gas wells, for amounts paid or incurred on or after January 1, 2024.

Effective/Operative Date

This provision, as part of a bill providing for an appropriation relating to the Budget Bill, would be effective upon enactment and operative for amounts paid or incurred on or after January 1, 2024.

Federal/State Law

Existing federal law allows taxpayers to deduct intangible drilling and development costs in the case of oil, gas, and geothermal wells.

Under the PITL, California conforms to IRC section 263, as of the "specified date" of January 1, 2015, allowing taxpayers to deduct intangible drilling and development costs in the case of oil, gas, and geothermal wells. Under the CTL, California has standalone language that allows taxpayers to deduct intangible drilling and development costs for oil and gas wells.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

None noted.

PROGRAM BACKGROUND

None noted.

OTHER STATES' INFORMATION

None noted.

FISCAL IMPACT

The FTB anticipates combined one-time costs for Provisions 5 and 8 of up to $200,000.

ECONOMIC IMPACT

Revenue Estimate

This provision would result in a revenue gain. In accordance with the bill provisions, staff defers to the DOF to determine the revenue impact of this provision.

LEGAL IMPACT

None noted.

EQUITY IMPACT

None noted.

Analysis Provision No. 6:

Conformity to Provisions Related to Charitable Deductions for Qualified Conservation Easement Contributions (Sections 21, 22, 29, 30, and 35 of the Bill)

This provision of the bill, under the PITL and CTL, for contributions made on or after January 1, 2024, would conform to federal charitable contribution rules regarding qualified conservation contributions for pass-through entities. These rules generally disallow qualified conservation contribution deductions if the amount of contribution made by a partnership exceeds 2.5 times the sum of each partner's relevant basis in the partnership.

However, certain qualified conservation contributions made by a partnership that exceed 2.5 times the sum of each partner's relevant basis in the partnership are allowed if they are for the preservation of a certified historic structure and the partnership provides a statement on their tax return disclosing that they made the contribution and provides the information as required by the Secretary of the Treasury (Secretary). The provision would also conform to the specified exceptions to the general rule. The provisions would apply in the same way to S corporations and other pass-through entities.

The provision would also allow donors the opportunity to amend an easement deed per the published safe harbor deed language.

In addition, under the AFITL, the provision would apply the ARP to the underpayment resulting from the disallowance of the deduction explained above, including requiring the FTB to disclose certain information regarding the ARP on notices sent to appropriate taxpayers. For purposes of computing the ARP, the resulting underpayment would be considered a gross valuation misstatement and the ARP applicable to that portion of the underpayment would be increased from 20 percent to 40 percent. The imposition of the ARP resulting from the disallowance of the deduction explained above would not require approval in writing by the immediate supervisor of the individual making the determination or a higher-level official as designated by the executive officer or the officer's delegee.

The reasonable cause exception to the ARP would not apply if the underpayment is due to the disallowance of the deduction explained above. In addition, for disallowed deductions, the provision would apply the same statute of limitations as applies under California law for abusive tax avoidance transactions.

Effective/Operative Date

This provision, as part of a bill providing for appropriations relating to the Budget Bill, would be effective immediately upon enactment and specifically operative for contributions made on or after January 1, 2024, for the deduction provisions; for returns filed on or after January 1, 2024, for the penalty provision; and for additions to tax imposed on or after January 1, 2024, for the reporting provision.

Federal/State Law

Federal Law

Generally, federal law allows for taxpayers to take a deduction from income for charitable contributions made to qualified charitable organizations within a taxable year. However, certain charitable deductions for qualified conservation contributions made by partnerships and other pass-through entities are disallowed, unless the entity that makes the contribution attaches a statement to their tax return for the taxable year providing information required by the Secretary.

The reporting requirements apply to any qualified conservation contribution made by a partnership or any other pass-through entity for the purpose of preserving any certified historical structure in which the contribution exceeds 2.5 times the sum of each partner's relevant basis. A certified historical structure is any building, structure or land that is listed on the National Register or is in a registered historic district and is certified by the Secretary as being of historical significance to the district.

The general limitation on the deduction for qualified conservation contributions made by a partnership or pass-through entity is that the contribution will not be treated as a qualified conservation contribution if the contribution amount exceeds 2.5 times the sum of each partner's relevant basis in the partnership. Relevant basis means, with respect to each partner, the portion of a partner's modified basis in the partnership that is allocable to a portion of the real property contributed. A partner's modified basis, with respect to each partner, is the partner's adjusted basis in the partnership immediately before the contribution, without regard to certain liabilities, and after taking into consideration any other adjustment as prescribed by the Secretary.

However, there are a few exceptions to the general limitation rule. The general rule, does not apply under the following circumstances:

1. The contribution was made at least three years after the holding period.
2. The contribution was made by a family partnership, if the interest in the partnership is held, directly or indirectly, by an individual or members of the family of such individual.
3. The qualified conservation contribution was made for the purpose to preserve any building which is a certified historical structure.

If a deduction for a charitable conservation contribution is disallowed, as specified, an ARP will apply for any underpayment of tax resulting from the disallowance. Generally, the ARP is 20% of the portion of underpayment of tax due, unless the portion of the underpayment is attributable to one or more gross valuation misstatements, then the penalty is increased to 40%. The portion of the underpayment attributable to any disallowance of a deduction for a charitable conservation contribution, as specified, is considered a gross valuation misstatement and the penalty applicable to that portion of the underpayment is increased to 40%. The reasonable cause exception for any underpayment due to the disallowance of conservation contributions will not apply.

For purpose of the federal statute of limitations to assess additional tax, if a deduction for a charitable conservation contribution is disallowed, it is treated as a transaction specifically identified by the Secretary as a tax avoidance transaction. A tax avoidance transaction is a reportable transaction. A reportable transaction is any transaction that requires the disclosure of information to be included in a tax return or statement for which the Secretary has determined to have potential for tax avoidance or evasion. When a tax avoidance transaction has been identified, the statute of limitations is extended. Generally, under federal law deficiency assessments are assessed within three years after a tax return has been filed. However, in cases that involve reportable transactions the time period for assessment of any imposition of tax or making adjustments does not expire before the first year after the information has been furnished to the Secretary.

Lastly, federal law provides an opportunity for a donor to correct certified deed errors and has safe harbor language for extinguishment clauses and boundary line adjustments.

State Law

Under the PITL, generally California conforms to the federal charitable contribution rules under the IRC as of the "specified date" of January 1, 2015. However, there are continuing differences between California and federal income tax laws. Under the CTL, California does not conform to the federal charitable contribution rules, but instead has standalone law that is generally similar to federal law that allows corporations a deduction for charitable contributions. However, there is no similar California provision that disallows contribution deductions that exceed the sum of each partner's relevant basis.

Under the AFITL, California has modified conformity to IRC section 6662, related to the ARP, as of the "specified date" of January 1, 2015. There is no provision under the ARP penalty that applies specifically for underpayments resulting from the disallowance of a charitable deduction for qualified conservation contributions.

Additionally, California does not conform to the statute of limitations under federal law regarding the assessment time period for the imposition of tax or making adjustments as of the "specified date" of January 1, 2015. California generally proposes deficiency assessments within 4 years after a return has been filed, except for cases that involve false or fraudulent tax returns and abusive tax avoidance transactions. The statute of limitations for proposed assessments for abusive tax avoidance transactions is generally within 12 years after a tax return is filed.

Lastly, current state law requires the FTB to disclose information related to an assessed penalty on a notice to the taxpayer, including upon taxpayer's request, the computation of the penalty. In general, an ARP may only be assessed upon approval of an immediate supervisor or a higher-level official as designated by the executive office, unless the ARP results from a federal change or correction required to be reported to the FTB pursuant to RTC section 18622.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

No legislation similar to this provision has been identified.

PROGRAM BACKGROUND

None noted.

OTHER STATES' INFORMATION

None noted.

FISCAL IMPACT

The FTB anticipates minimal costs to implement this provision.

ECONOMIC IMPACT

Revenue Estimate

The provision of this bill as amended on June 10, 2024, as they relate to Conservation Easements conformity would result in a revenue gain.

In accordance with these provisions staff defers to the DOF to determine the revenue impact. The penalty provisions of the bill would not impact state income or franchise tax revenue.

LEGAL IMPACT

None noted.

EQUITY IMPACT

None noted.

Analysis Provision No. 7:

NOL Suspension (Sections 23 and 36 of this Bill)

This provision would disallow NOL deductions by suspending them for taxable years 2024, 2025, and 2026 for a taxpayer. The following taxpayers would be subject to the NOL suspension:

- Under the PITL, those with modified adjusted gross income (AGI) or net business income of $1,000,000 or more, and
- Under the CTL, those with income subject to tax of $1,000,000 or more.

This provision would also extend the NOL carryover period by one year for NOLs incurred in taxable year 2025, two years for NOLs incurred in taxable year 2024, and three years for NOLs incurred in taxable years beginning before 2024.

"Modified adjusted gross income" would mean the amount required to be shown as AGI 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.

Effective/Operative Date

This provision, included within a bill providing for appropriations relating to the Budget Bill, would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2024, and before January 1, 2027.

Federal/State Law

Federal Law

An 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 Coronavirus Aid, Relief, and Economic Security Act (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. (CARES Act (HR748; Public Law 116-136).) 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).)

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.

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 AGI 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, was 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 and 2021, California again suspended the NOL carryover deduction. The suspension of NOLs did not apply to a taxpayer:

- Under the PITL, with modified AGI or net business income of less than $1 million.
- Under the CTL, with income subject to tax of less than $1 million.

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

SB 113 (Senate Committee on Budget and Fiscal Review, Chapter 3, Statutes of 2022), under the PITL and CTL, amongst other provisions, repealed the suspension of NOL deductions for the 2022 taxable year.

AB 85 (Assembly Committee on Budget, Chapter 8, Statutes of 2020), a budget trailer bill, amongst other provisions, suspended the use of NOL deductions. The suspension applied to taxpayers with modified AGI of less than $1 million under the PITL or for taxpayers with net business income subject to tax under the CTL of less than $1 million 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.

PROGRAM BACKGROUND

None noted.

OTHER STATES' INFORMATION

None noted.

FISCAL IMPACT

The FTB anticipates minimal costs to implement this provision.t

ECONOMIC IMPACT

Revenue Estimate

This provision would result in a revenue impact. In accordance with the bill provisions, staff defers to the DOF to determine the revenue impact of this bill.

LEGAL IMPACT

None noted.

EQUITY IMPACT

None noted.

Analysis Provision No. 8:

Repeal of the Percentage Depletion Method for Oil and Gas Well Producers: (Sections 24, 25, 26, 38, 39, and 40 of this Bill)

Sections 24 and 38 of this bill would, under the PITL and CTL, for taxable years beginning on or after January 1, 2024, repeal the calculation of depletion as a percentage of gross income from property used for oil shale and coal mining. In addition, this provision would repeal the depletion percentage exemptions and limitations under IRC section 613A for oil and gas wells.

Sections 25, 26, 39 and 40 of this bill would, under the PITL and CTL, for taxable years beginning on or after January 1, 2024, include technical clean-up to remove RTC sections referencing IRC section 613A that became obsolete due to the amendments discussed above.

Effective/Operative Date

This provision, included within a bill providing for appropriations relating to the Budget Bill, would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2024.

Federal/State Law

Federal Law

A taxpayer is permitted a reasonable allowance for depletion in the case of mines, oil and gas wells, other natural deposits, and timber. The taxpayer is allowed a depletion deduction if the taxpayer owns an "economic interest" in the natural resource. An owner of an "economic interest" includes an owner-operator, a lessor or lessee, an owner of a royalty interest or retained net profits interest, and an owner of a production payment that is not treated as a mortgage loan.

There are two depletion methods: (1) Cost depletion, and (2) Percentage depletion.

Cost Depletion: This method is similar to the units-of-production depreciation method in which the depreciation is related to the level of the output during each period in

comparison to the total output possible during the depreciable life of the asset. Cost depletion starts by computing the basis per recoverable unit of the natural resource, and the depletion allowance for any given period is computed by multiplying the basis per recoverable unit by the number of units produced in that period.

Percentage Depletion: In percentage depletion, the gross possible income from the property is amortized over the life of the property, in contrast to the amortization of the cost that is used in depreciation and in cost depletion. Gross income from the property, therefore, needs to be computed before determining the percentage depletion. Also, because the depletion is on the basis of the income as opposed to the cost, it is possible that the total depletion can exceed the total cost of the property.

In general, a taxpayer is allowed a percentage depletion deduction, as a percentage of gross income, for property used in mining, wells, and other natural deposits. Gross income excludes any rents or royalties paid or incurred by the taxpayer in respect to the property. The percentage depletion deduction is limited to 50% of a taxpayer's taxable income from the property. While taxpayers engaged in the production of oil and gas are allowed a percentage depletion deduction of up to 100% of their taxable income from the property. Taxable income is computed without the allowance for depletion and without any qualified income deductions under IRC section 199A. The percentage depletion rates for oil shale and coal are 15% and 10%, respectively.

IRC section 613A provides the following exemptions and limitations for taxpayers involved in the production of oil and gas:

- An exemption is provided for taxpayers of domestic gas wells that produce regulated natural gas and are sold under a fixed contract. These taxpayers may claim a percentage depletion deduction of 22% of gross income from the property, not to exceed 100% of taxable income from the property for the taxable year.
- An exemption is provided for taxpayers who produce natural gas by geopressured brine. These taxpayers may claim a percentage depletion deduction of 10% of gross income from the property, not to exceed 100% of taxable income from the property for the taxable year.
- An exemption is provided to independent producers and royalty owners who may claim the percentage depletion deduction. The depletion deduction is 15% of the gross income from the property, not to exceed 65% of the taxable income from the property for the taxable year. This exemption excludes certain refiners engaged in refining crude oil from taking a percentage depletion deduction if their average daily refinery runs exceed 75,000 barrels for the taxable year.

Prior to 2005, under IRC section 613A, the limitations on percentage depletion for independent producers and royalty owners did not apply to certain refiners of crude oil whose average daily refinery runs for the taxable year exceeded 50,000. The average daily refinery runs for the taxable year are computed by dividing the aggregate refinery runs for the taxable year by the number of days in the taxable year.

In 1997, IRC section 613A(c)(6)(H) was added to temporarily suspend the taxable income limitations on the production of domestic crude oil and natural gas from marginal properties. This provision allowed for independent producers and royalty owners to take a percentage depletion deduction up to 100% of their taxable income for the year. This section applied to taxable years beginning after December 31,1997, and before January 1, 2008, or beginning after December 31, 2008, and before January 1, 2012. In 2018, this section was deleted from the IRC.

State Law

California law generally conforms to the IRC as of the "specified date" of January 1, 2015, with respect to the percentage depletion deduction for mines, oil and gas wells, other natural deposits.

California does not conform to the temporary suspension of the taxable income limitations on the production of domestic crude oil and natural gas from marginal properties. California also does not conform to the changes made by Public Law 109-58 to IRC section 613A(d)(4), that increased the threshold for exclusion of certain refiners from the limitations on percentage depletion for oil and gas wells.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

ABX3-30 (Calderon, 2007/2008), would have disallowed the percentage depletion for any trade or business engaged in the oil production business for taxable years beginning on or after January 1, 2008. ABX3-30 did not pass out of Assembly by the constitutional deadline.

PROGRAM BACKGROUND

None noted.

OTHER STATES' INFORMATION

None noted.

FISCAL IMPACT

The FTB anticipates combined one-time costs for provisions 5 and 8 of up to $200,000.

ECONOMIC IMPACT

Revenue Estimate

This provision would result in a revenue gain. In accordance with the bill provisions, staff defers to the DOF to determine the revenue impact of this bill.

Revenue Discussion

This provision would disallow, for taxable years beginning on or after January 1, 2024, the calculation of depletion as a percentage of gross income from the property for oil and gas producers.

LEGAL IMPACT

None noted.

EQUITY IMPACT

None noted.

Analysis Provision No. 9:

Extension of Electronic Communications (Section 27 of this bill)

This provision would eliminate the repeal date for FTB to implement an alternative communication method, at the request of a taxpayer or the taxpayer's representative, to provide certain notifications to the taxpayer or their representative in a preferred electronic communication method designated by the taxpayer that a notice, statement, bill, or other communication is available in their taxpayer folder on FTB's internet website. This provision would also eliminate the repeal date for the authorization for a taxpayer or their representative to file a protest, notification, or provide another communication to FTB in a secure manner.

Effective/Operative Date

This provision, as part of a bill providing for an appropriation relating to the Budget Bill, would be effective and operative immediately upon enactment.

AB 3287 (Assembly Committee on Revenue and Taxation, Chapter 122, Statutes of 2024), containing the same language as this provision, was chaptered on July 15, 2024. AB 3287 was chaptered after this bill and will take effect on January 1, 2025. As a result, the identical version of this provision in AB 3287 would chapter out the changes made by this provision on January 1, 2025.

Federal/State Law

Federal Law

The Internal Revenue Service (IRS) allows a taxpayer to create an online account through which the taxpayer may elect to receive an email when there is a new notice in their online account. In addition, a taxpayer can view their account balances, personal information, payment information, and digital copies of past IRS notices. A taxpayer can also select an electronic payment option, set up an online payment agreement, access tax records, and approve and electronically sign a Power of Attorney and Tax Information Authorization requests from their tax professional.

State Law

Current state law (RTC section 18416.5) allows the FTB to provide alternative communication methods at the request of a taxpayer or the taxpayer's authorized representative to provide a notice, statement, bill, or other communication via electronic means. However, this law will cease to be operative for a notice, statement, bill, protest, or other communication between FTB and a taxpayer on or after January 1, 2025.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

AB 3287 (Assembly Committee on Revenue and Taxation, Chapter 122, Statutes of 2024) eliminated the repeal date for the FTB's authorization to, at the request of the taxpayer, send notifications electronically. AB 3287 will take effect on January 1, 2025.

AB 1720 (Assembly Revenue and Taxation Committee, Chapter 177, Statutes of 2017) extended the repeal date for the FTB's authorization to, at the request of the taxpayer, send notifications electronically from January 1, 2018, to January 1, 2025.

AB 2177 (Beall, Chapter 136, Statutes of 2010), beginning January 1, 2011, and ending on January 1, 2018, allowed a taxpayer to elect to receive electronic communications from the FTB.

PROGRAM BACKGROUND

Since 2011, California has allowed a taxpayer or their representative to choose to receive certain notifications in an electronic format. This election originally had a repeal date of January 1, 2018. In 2017, this repeal date was extended to January 1, 2025. Approximately 1 million taxpayers have registered for a MyFTB account. Out of those 1 million taxpayers, approximately 50,000 have chosen to receive an electronic notification rather than receiving a notice via United States mail. For fiscal year 2022/2023, approximately 110,000 emails were sent to taxpayers advising them that they had a notice available online in their MyFTB account. Taxpayers can also elect to receive a text message notification in addition to or in lieu of receiving an email notification. For fiscal year 2022/2023, approximately 65,000 text messages were sent to taxpayers advising them that they had a notice available in their MyFTB account.

OTHER STATES' INFORMATION

None noted.

FISCAL IMPACT

This provision would not significantly impact FTB's costs.

ECONOMIC IMPACT

Revenue Estimate

This provision would not impact state income or franchise tax revenue.

LEGAL IMPACT

None noted.

EQUITY IMPACT

None noted.

Analysis Provision No. 10:

State of Emergency Declarations (Section 28 of this Bill)

This provision would provide that the Director of Finance has the authority to determine whether a taxpayer is affected by a state of emergency, and whether tax deadlines should be postponed due to a state of emergency.

Moreover, "impacted taxpayers" would be provided postponement of tax-related deadlines, as prescribed under IRC section 7508A, during an "additional relief period."

The provision defines the following terms:

"Additional relief period" would mean the period beginning on the date the state postponement period expires, if any, and ending on the date the federal postponement period expires.

“Federal postponement period” means the period, up to one year, that the IRS postpones deadlines for performing tax-related acts under IRC section 7508A.

“State postponement period” is the period determined by the Director of Finance.

"Impacted taxpayer" would mean a taxpayer that meets both of the following:

- The taxpayer qualifies for relief under IRC section 7508A, with respect to a federally declared disaster or a taxpayer determined by the Director of Finance to be affected by a state of emergency, but didn’t file their California tax return or make payments of tax or fees required before the expiration of the state postponement date and
- The taxpayer requests relief and provides supporting documentation.

"Supporting documentation" would mean:

- A letter from the Federal Emergency Management Agency that approves assistance to the impacted taxpayer pursuant to the federal Robert T. Stafford Disaster Relief and Emergency Assistance Act (42 U.S.C. Sec. 5121 et seq.).
- A determination of award letter from the Small Business Administration disaster loan program that approves assistance to the impacted taxpayer.

- A statement, signed under penalty of perjury, from a tax professional indicating the impacted taxpayer's books and records that are necessary to meet a tax deadline were destroyed in the disaster area or jurisdiction for which the Governor has proclaimed a state of emergency.
- A law enforcement report issued to the impacted taxpayer, related to theft or looting due to lawlessness occurring during the disaster or emergency and in the disaster area or jurisdiction for which the Governor proclaimed a state of emergency.
- An insurance claim submitted by or on behalf of the impacted taxpayer, related to the disaster or conditions of emergency.
- Verification of disaster relief related to housing assistance, property damage, employment, public health, mortgage assistance, or business operation received from a government entity, banking institution, or organization described in Section 501(c)(3) of the IRC.

The provision would also authorize FTB to adopt regulations that are necessary and appropriation to implement the provision. However, the APA would not apply to any standard, criterion, procedure, determination, rule, notice, guideline, or any other guidance established by the FTB pursuant to this provision.

Effective/Operative Date

As a provision within a bill providing for an appropriation related to the Budget Bill, this provision would be effective immediately upon enactment and specifically operative for any federally declared disaster or Governor-proclaimed state of emergency on or after the effective date of the bill.

Federal/State Law

Federal Law

Under federal law, the Secretary of the Treasury determines whether a taxpayer is affected by a federally declared disaster, significant fire, or terroristic or military action. For such affected taxpayers, the Secretary of the Treasury may specify a period of up to 1 year that may be disregarded in determining, with respect to any tax liability, whether the following acts (in addition to others) were timely performed:

- Filing a return.
- Payment of tax or an installment payment.
- Filing a claim for credit or refund of tax.
- Filing a petition with the Tax Court, or a notice of appeal from a Tax Court decision.

The Secretary may disregard up to 1 year in determining the amount of interest, penalty, additional amount, additional tax, credit, or refund.

"Qualified taxpayers" are provided a mandatory 60-day extension on tax liabilities beginning on the earliest incident date and ending 60 days after the later of the earliest incident date or the date of the declaration of a federally declared disaster.

"Qualified taxpayer" means—

- any individual whose principal residence is in a disaster area,
- any taxpayer if the taxpayer's principal place of business (other than the business of performing services as an employee) is in a disaster area,
- any individual who is a relief worker affiliated with a recognized government or philanthropic organization and who is assisting in a disaster area,
- any taxpayer whose records necessary to meet a deadline for an act described in IRC section 7508(a)(1) (e.g., armed forces personnel's records required for the filing of tax returns, payment of taxes, or filing a tax appeal) are maintained in a disaster area,
- any individual visiting a disaster area who was killed or injured as a result of the disaster, and
- solely with respect to a joint return, any spouse of an individual described in any preceding subparagraph of this paragraph.

State Law

Current state law conforms to IRC section 7508A, relating to postponement of tax-related deadlines, due to a federally declared disaster, and applies IRC section 7508A to a taxpayer determined by the FTB to be affected by a state of emergency declared by the Governor.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

SB 264 (Niello, Chapter 285, Statutes of 2023), under the PITL and CTL, extended the deduction for disaster losses to taxable years beginning before January 1, 2029, and extended the provision prohibiting any law that suspends, defers, reduces, or otherwise diminishes the deduction of an NOL from applying to these disaster losses.

SB 35 (Wolk and Dodd, Chapter 230, Statutes of 2015) allowed, under the PITL and CTL, disaster loss treatment for losses sustained in an area declared by the Governor to be a state of emergency.

PROGRAM BACKGROUND

None noted.

OTHER STATES' INFORMATION

None noted.

FISCAL IMPACT

The FTB anticipates minimal costs to implement this provision.

ECONOMIC IMPACT

Revenue Estimate

In accordance with the bill provisions, staff defers to the DOF to determine the revenue impact of this provision.

LEGAL IMPACT

None noted.

EQUITY IMPACT

None noted.

Analysis Provision No. 11:

Terminate the Delinquent Tax Collection Fund (Section 31 of this Bill)

This provision would, under the AFITL, repeal the Delinquent Tax Collection Fund on June 30, 2024. Thus, eliminating FTB's requirement to determine the amount of contracting costs incurred for the collection of delinquent accounts and the Controller's requirement to transfer that amount from the Personal Income Tax Fund or the Corporation Tax Fund to the Delinquent Tax Collection Fund.

Effective/Operative Date

This provision, included within a bill providing for appropriations relating to the Budget Bill, would be effective immediately upon enactment.

Federal/State Law

Federal Law

No comparable provision in federal law.

State Law

Current state law provides that the FTB may enter into agreements with one or more persons for the purposes of collecting delinquent accounts for amounts imposed under Part 10, Part 10.2, or Part 11 of the RTC. Upon FTB notifying the Controller of the contracting cost incurred for the collection of delinquent accounts, the Controller is required to transfer from the Personal Income Tax Fund or the Corporation Tax Fund to the Delinquent Tax Collection Fund. The Controller shall then transfer the amount for contracting cost incurred from the Delinquent Tax Collection Fund to the FTB for reimbursement. Funds remaining in the Delinquent Tax Collection Fund are then transferred to either the Personal Income Tax Fund or the Corporation Tax Fund.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

SB 3 (Greene, Chapter 31, Statutes of 1993) amongst other provisions, provided that the FTB may enter into agreements with one or more persons for the purposes of collecting delinquent accounts for specified amounts imposed. Additionally, required the Controller to reimburse the FTB for contracting costs, as specified.

PROGRAM BACKGROUND

None noted.

OTHER STATES' INFORMATION

None noted.

FISCAL IMPACT

The FTB anticipates minimal costs to implement this provision.

ECONOMIC IMPACT

Revenue Estimate

This provision, as amended June 10, 2024, does not change the way income or franchise tax is calculated under the RTC.

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.

LEGAL IMPACT

None noted.

EQUITY IMPACT

None noted.

Analysis Provision No. 12:

Extend the Strategic Aircraft Credit's Ability to Reduce Tax Below TMT (Section 32 of this Bill)

This provision would, under the CTL, extend the taxpayer's ability to reduce tax below the TMT by the Strategic Aircraft Credit for five years from taxable years beginning on or after January 1, 2020, and before January 1, 2026, to taxable years beginning before January 1, 2020, and before January 1, 2031.

Effective/Operative Date

This provision, as part of a bill providing for appropriations relating to the Budget Bill, would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2026, and before January 1, 2031.

Federal/State Law

Federal Law

The federal corporate alternative minimum tax (AMT) was repealed by the federal Tax Cuts and Jobs Act for taxable years beginning after December 31, 2017.

State Law

Under current state law, corporations are subject to tax that includes both the regular tax and the AMT if their TMT is greater than their regular tax. Under current law, a number of credits are specifically allowed to reduce tax below the TMT. The Strategic Aircraft Credit may reduce the tax below the TMT for taxable years beginning on or after January 1, 2020, and before January 1, 2026. The Strategic Aircraft Credit allows a credit in the amount of wages paid or incurred for qualified full-time employees that are employed in this state to design, test, manufacture, or support the production of property for the use in, or as a component of, a new advanced strategic aircraft for the United States Air Force.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

AB 85 (Committee on Budget, Chapter 8, Statutes of 2020) among other things, under the CTL, allowed the Strategic Aircraft Credit to reduce tax below the TMT for taxable years beginning on or after January 1, 2020, and before January 1, 2026.

PROGRAM BACKGROUND

None noted.

OTHER STATES' INFORMATION

None noted.

FISCAL IMPACT

The FTB anticipates minimal costs to implement this provision.

ECONOMIC IMPACT

Revenue Estimate

State privacy rules do not allow disclosure of revenue estimates for proposals that would affect fewer than ten taxpayers.

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.

LEGAL IMPACT

None noted.

EQUITY IMPACT

None noted.

Analysis Provision No. 13:

Apportionment Formula (Section 41 of the Bill)

This provision would, under the CTL, exclude from the apportionment formulas used under the CTL, any transaction or activity to the extent that it generates income or loss not included in net income. The provision defines "not included in net income'" as income from transactions and activities that are not included in net income subject to apportionment for any reason, including, but not limited to, exclusion, deduction, exemption, elimination, or nonrecognition.

This provision also finds that it is the intent of the Legislature that the FTB's Legal Ruling 2006-1, Apportionment Factor Treatment of Exempt Income, dated April 28, 2006, would apply with respect to the apportionment formula of taxpayers subject to CTL. The provision would provide that this is declaratory of existing law.

This provision would allow FTB to adopt regulations as necessary or appropriate to carry out the purpose of this provision. The rulemaking procedures under the APA (Government Code section 11340 et seq.) would not apply to any regulation, standard, criterion, procedure, determination, rule, notice, guideline, or any other guidance provided by the FTB to carry out the purpose of this provision.

Effective/Operative Date

As a provision within a bill providing for an appropriation related to the Budget Bill, this provision would be effective immediately upon enactment and as a declaration of existing law, would apply to taxable years beginning before, on, or after the effective date of the act adding this provision.

Federal/State Law

Federal Law

No comparable provision in federal law.

State Law

California adopted the Uniform Division of Income for Tax Purposes Act (UDITPA) in 1966, which is the basis for determining the extent to which the income of multistate and multinational corporations may be attributed to the state by means of allocation of nonbusiness income and apportionment of business income. State law uses an apportionment formula to determine the amount of "business" income attributable to California. "Business income attributable to California" is a taxpayer's "business income" multiplied by its California apportionment formula. RTC section 25120(a) defines "business income" as income arising from transactions and activities in the regular course of the taxpayer's trade or business and includes income from tangible and intangible property if the acquisition, management, and disposition of the property constitute integral parts of the taxpayer's regular trade or business operations.

Under current state law, all business income of an apportioning trade or business, other than an apportioning trade or business that derives more than 50% of its gross business receipts from conducting agricultural, extractive, savings and loan, or banking or financial business activities, is apportioned to California by multiplying the business income by the sales factor. Business income of an apportioning trade or business that derives more than 50% of its gross business receipts from conducting agricultural, extractive, savings and loan, or banking or financial business activities is apportioned to California by multiplying business income by a three-factor formula consisting of property, payroll, and sales, as specified. Each of these factors is represented as a fraction. For the sales factor, generally the numerator is the gross receipts from sales sourced to California and the denominator is the total gross receipts from sales. The factor, as a percentage, is applied against an apportioning business entity's business income to determine the amount of business income apportioned to California.

In addition, when a taxpayer receives income that is partially or completely excluded from the measure of income or franchise tax, the activities related to that income would also be excluded for purposes of the apportionment factor. (FTB Legal Ruling 2006-01, dated April 28, 2006, Apportionment Factor Treatment of Exempt Income.)

Under current law, as explained in FTB Legal Ruling 2006-01, the income and factors of entities exempt from the franchise and income tax, such as insurance companies, are excluded from the apportionment formula. Furthermore, the activities that give rise to nonbusiness income are excluded from the apportionment formula because nonbusiness income is allocated and not apportioned. Therefore, for the purpose of determining the sales factor used in the apportionment of business income, the sales factor calculation does not include activities related to the production of nonbusiness income. Under current law, as explained in FTB Legal Ruling 2006-01, gross receipts that are exempt from taxation must be removed from both the numerator and denominator of the apportionment formula. Income items which are proportionally exempt from tax must be proportionally removed from the apportionment formula. Where activities support both the production of taxable business income and excluded income, such activities must be separated into parts with one part included in the apportionment formula and the other excluded.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

AB 820 (Cooley, et al., 2021/2022), among other things, would have required, for taxable years beginning on or after January 1, 2022, and before January 1, 2027, a savings and loan and banking or financial business to exclude qualified interest from its calculation of the sales factor under the three-factor formula. This bill did not pass out of the Assembly Appropriations Committee by the constitutional deadline.

PROGRAM BACKGROUND

None noted.

OTHER STATES' INFORMATION

None noted.

FISCAL IMPACT

The FTB anticipates minimal costs to implement this provision.

ECONOMIC IMPACT

Revenue Estimate

This provision would result in a revenue impact. In accordance with the bill provisions, staff defers to the DOF to determine the revenue impact of this provision.

Revenue Discussion

This provision provides that any transaction or activity, to the extent that it generates income or loss not included in net income subject to apportionment, is excluded from the California apportionment formulas under the CTL. Not included in net income, is defined as income from transactions and activities that is not included in net income subject to apportionment for any reason, including, but not limited to, exclusion, deduction, exemption, elimination, or nonrecognition.

LEGAL IMPACT

None noted.

EQUITY IMPACT

None noted.

Analysis Provision No. 14:

MCTR Clarification (Section 43 of this Bill)

This provision would, under the WIC, clarify that any unexpended or unclaimed balance of MCTR payments would be returned to the FTB. The FTB would be required to deposit the moneys in the General Fund.

Effective/Operative Date

This provision, as part of a bill providing for an appropriation relating to the Budget Bill, would be effective and operative immediately upon enactment.

Federal/State Law

Federal Law

No comparable provision in federal law.

State Law

Under the WIC, the Golden State Stimulus I (GSS I), Golden State Stimulus II (GSS II), and Better for Families Act (also known as MCTR) payments were issued as separate, one-time payments to qualified recipients. Qualified recipients had to meet specified eligibility requirements to receive a payment.

For the MCTR payments, California contracted with a third-party vendor for services related to the distribution of payments. The payments were required to include an expiration date of no later than April 30, 2026. Upon expiration, any unexpended or unclaimed balance of the payments were required to be returned to the state, and all unused balances returned, no later than May 31, 2026.

Implementation Considerations

None noted.

Technical Considerations

None noted.

Policy Considerations

None noted.

LEGISLATIVE HISTORY

SB 131 (Senate Committee on Budget, Chapter 55, Statutes of 2023) required the FTB to make MCTR payments to qualified recipients no later than September 30, 2023, and allowed the FTB to reissue stale, dated, replacement warrants or replacement debit cards through third-party vendors after September 30, 2023.

AB 192 (Assembly Committee on Budget, Chapter 737, Statutes of 2022) established the Better for Families Act under the WIC that authorized the Controller to make a one-time MCTR payment to qualified recipients in an applicable amount, which is excluded from gross income for California purposes.

PROGRAM BACKGROUND

None noted.

OTHER STATES' INFORMATION

None noted.

FISCAL IMPACT

This provision would not significantly impact the FTB's costs.

ECONOMIC IMPACT

Revenue Estimate

This provision as amended June 10, 2024, would not impact state income or franchise tax revenue.

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

LEGAL IMPACT

None noted.

EQUITY IMPACT

None noted.

APPOINTMENTS (All Provisions)

None noted.

SUPPORT/OPPOSITION (All Provisions)

Support:

None on file.

Opposition:

None on file.

ARGUMENTS (All Provisions)

Proponents:

None on file.

Opponents:

None on file.

LEGISLATIVE CONTACT

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