SCS Agency
Franchise Tax Board

SUMMARY ANALYSIS OF AMENDED BILL

Author:	Hayden	Analyst:	Roger Lackey	Bill Number:	SB 1435
Related Bills:	See Prior Analysis	Telephone:	845-3627	Amended Date:	03-26-98
		Attorney:	Doug Bramhall	Sponsor:	

SUBJECT: Minimum Franchise Tax/ Change From $600 to $300 For Qualified New Corporations On Or After January 1, 1998

_____ DEPARTMENT AMENDMENTS ACCEPTED. Amendments reflect suggestions of previous analysis of bill as introduced/amended _________.

__X__ AMENDMENTS IMPACT REVENUE. A new revenue estimate is provided.

_____ AMENDMENTS DID NOT RESOLVE THE DEPARTMENT'S CONCERNS stated in the previous analysis of bill as introduced/amended _________.

_____ FURTHER AMENDMENTS NECESSARY.

_____ DEPARTMENT POSITION CHANGED TO _________________________.

__X__ REMAINDER OF PREVIOUS ANALYSIS OF BILL AS INTRODUCED January 26, 1998 STILL APPLIES.

__X__ OTHER - See comments below.

SUMMARY OF BILL

For income years beginning on or after January 1, 1998, this bill would reduce the minimum franchise tax to $300 for the first two income years, which includes the initial prepayment to the Secretary of State (SOS), for any domestic bank or corporation incorporated on or after January 1, 1998, with gross receipts of less than $1 million for the income year.

SUMMARY OF AMENDMENT

The March 26, 1998, amendment provided for a reduced minimum franchise tax of $300, for a "qualified new corporation," as discussed in this analysis.

The amendment also deleted the language providing a reduced minimum franchise tax amount, as determined by the Bureau of State Audits, for a "qualified small business."

Except for the discussion in this analysis, the department's analysis of SB 1435, as introduced January 26, 1998, still applies.

SPECIFIC FINDINGS

This bill would reduce the minimum franchise tax from $800 to $300 for the first

DEPARTMENTS THAT MAY BE AFFECTED:

____ STATE MANDATE　　　____ GOVERNOR'S APPOINTMENT

Board Position:	Agency Secretary Position:	GOVERNOR'S OFFICE USE
____ S　____ O ____ SA　____ OUA ____ N　_X_ NP ____ NA　____ NAR ________ PENDING	____ S　____ O ____ SA　____ OUA ____ N　____ NP ____ NA　____ NAR DEFER TO ____________	Position Approved ____ Position Disapproved ____ Position Noted ____
Department/Legislative Director　Date Johnnie Lou Rosas　4/1/98	Agency Secretary　Date	By:　Date:

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two income years (the year for the initial prepayment to the SOS and the immediately succeeding income year) for banks and corporations incorporated on or after January 1, 1998, with gross receipts, less returns and allowances reportable to this state, of less than $1 million for the income year.

This bill would reduce the prepayment to the SOS for qualified new corporations from $600 to $300.

This bill would require a qualified new corporation to pay an additional tax of $500 on the due date of its tax return, without regard to extension, if for the corporation's first or second income year its gross receipts exceed $1 million.

This bill would define a "qualified new corporation" as a business that begins operation at or after the time of its incorporation. A "qualified new corporation" would not include any business that began operation as a single proprietorship, a partnership, or any other form of business prior to its incorporation.

This bill would specify that the reduced minimum franchise tax does not apply to certain entities, including limited liability companies, limited liability partnerships, and subsidiaries.

This bill also would not apply to any bank or corporation that reorganized solely for the purpose of reducing its minimum franchise tax.

Policy Considerations

This bill provides that for a new bank or corporation to qualify as a "qualified new corporation," the bank or corporation must have begun operation at or after the time of its incorporation. Currently, newly incorporated banks or corporations that have operated in any other business form, such as a sole proprietorship, are eligible for the reduced minimum franchise tax of $600. Under this bill, these corporations would no longer qualify as a "qualified new corporation" and, as a result, each would owe an $800 minimum tax upon filing with the Secretary of State, a $200 tax increase.

Implementation Considerations

This bill would not allow subsidiaries to be eligible for the reduced minimum franchise tax. The term "subsidiary" is not defined. Amendment 8 would clarify the author's intent to prevent a corporation that is owned by another corporation to qualify for the reduced minimum franchise tax by defining "subsidiary."

Corporations that pay the $800 minimum franchise tax as their first estimate payment for the income year beginning on or after January 1, 1998, but at the end of the year have gross receipts of $1 million or less, would be eligible for a reduced minimum tax of $300. In addition, refunds also would have to be made to qualified new corporations that incorporated on or after January 1, 1998, and prepaid $600 to the SOS instead of $300. Issuing these refunds would create a minor additional workload for the department.

Also, this bill provides that only new banks or corporations that begin operation at or after the time of incorporation would qualify as a "qualified new corporation." It would be difficult for the department to verify whether each "qualified new corporation" had operated in another business form prior to its incorporation.

Technical Considerations

Amendments 1, 3, 4, 5, 6 and 7 delete the term "bank" which is unnecessary as banks are now included in the definition of "corporation."

Banks and corporations with gross receipts of less than $1 million would pay the reduced tax, while those with gross receipts which exceed $1 million would pay the additional $500. The bill is silent on taxpayers with gross receipts of exactly $1 million. Amendment 2 would change "less than $1 million" to "$1 million or less" to eliminate this gap.

This bill uses the term "single proprietorship," it is unclear what is a "single proprietorship." If it was the author's intent to use the term "sole proprietorship" not "single proprietorship," the language of the bill should be amended to provide for the author's intent.

FISCAL IMPACT

Tax Revenue Estimate

Revenue losses from this bill are estimated as follows:

Estimated Revenue Impact of SB 1435 As Amended March 26, 1998 Effective After December 31, 1997 Assumed Enactment After June 30, 1998			
1998-9	**1999-0**	**2000-1**	**2001-2**
($18)	($13)	($14)	($15)

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this measure.

Tax Revenue Discussion

Revenue losses would depend on the number of newly-formed businesses that incorporate and have gross receipts, less returns and allowances reportable to this state, of less than $1 million in one or both of its initial two years of doing business (counting the Secretary of State fee as payment for its initial year).

The total number of new incorporations projected for 1998 is 55,100 with approximately 50% having less than $1 million in gross receipts. The number qualifying as "newly-formed" entities is projected at 16,900 (60%), as estimated previously for SB 510 (April 15, 1997).

The larger 1998-9 impact reflects payment reductions for all of 1998 and the first half of 1999. For the SOS fee issue, it is assumed that initially all newly-formed entities would pay the lower Secretary of State fee, but those not meeting the gross receipts test would pay the difference at the end of the income year.

BOARD POSITION

No position.

At its March 26, 1998, meeting the Franchise Tax Board considered this bill but took no position: Julie Bornstein, on behalf of Controller Kathleen Connell, neutral; Member Dean Andal, support; and Robin J. Dezember, on behalf of Member Craig L. Brown, abstained.

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FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO SB 1435
As Amended March 26, 1998

AMENDMENT 1

On page 5, line 6, strikeout "bank or domestic"

AMENDMENT 2

On page 5, lines 7 and 8, strikeout "of less than one million dollars ($1,000,000)" and insert:

of one million dollars ($1,000,000) or less

AMENDMENT 3

On page 5, line 11, strikeout "domestic bank or"

AMENDMENT 4

On page 5, line 15, strikeout "banks or"

AMENDMENT 5

On page 5, lines 17 and 18, strikeout "bank or"

AMENDMENT 6

On page 5, line 21, strikeout "bank or"

AMENDMENT 7

On page 5, line 34, strikeout “bank or”

AMENDMENT 8

On page 6, amend lines 5 to 7, as follows:

Section 860D of the Internal Revenue Code, or to ~~the formation of~~ any subsidiary corporation, if 50 percent or more of its stock is, or will be upon the initial issuance of stock, owned by another corporation ~~to the extent applicable~~.