Franchise Tax Board

SUMMARY ANALYSIS OF AMENDED BILL

Author:	Lopez	Analyst:	Jessica Deitchman	Bill Number:	AB 2625
Related Bills	See Prior Analysis	Telephone:	845-6310	Amended Date	May 2, 2016
		Attorney:	Bruce Langston	Sponsor:	

SUBJECT: Annual Tax & Minimum Franchise Tax/Reduce First 5 Taxable Years for New Microbusiness

SUMMARY

This bill would, under the Personal Income Tax Law (PITL) and Corporation Tax Law (CTL), reduce the annual or minimum franchise tax imposed on certain new microbusiness entities.

RECOMMENDATION

No position.

SUMMARY OF AMENDMENTS

The May 2, 2016, amendments made technical changes and resolved most of the technical considerations discussed in the department's analysis of the bill as amended February 19 and April 6, 2016. Except for the "This Bill," and "Technical Considerations" sections, the department's analysis of the bill as introduced February 19, 2016 and amended April 6, 2016, still applies. The "Economic Impact" and "Fiscal Impact" sections are restated for convenience.

THIS BILL

For taxable years beginning on or after January 1, 2017, this bill would, under the PITL and CTL, reduce the amount of minimum franchise or annual tax imposed on a new microbusiness that is a limited partnership (LP), limited liability company (LLC), and limited liability partnership (LLP) for each of the first five years and for a corporation for its second, third, fourth, and fifth taxable years to the amounts shown in the table below:

Gross receipts of $50,000 or less	Gross receipts of $100,000 or less but more than $50,000	Gross receipts of $150,000 or less but more than $100,000	Gross receipts of more than $150,000
$200	$400	$600	$800

For any taxable year in which an LLC or corporation has qualified to pay a reduced annual tax, but has gross receipts, less returns and allowances, derived from or attributable to this state which exceed the amount specified for that reduced amount, an additional tax in an amount equal to $600, $400 or $200, as applicable, for that taxable year would be due and payable by the LLC or corporation on the due date of the return without regard to extension for that taxable year.

The bill would define the following terms:

- "Gross receipts, less returns and allowances" means the sum of the gross receipts from the production of business income and the gross receipts from the production of nonbusiness income.
    - "Gross receipts, less returns and allowances, derived from or attributable to this state" would be determined using the rules for assigning sales under current law and the regulations thereunder, as modified by regulations under Section 25137, other than those provisions that exclude receipts from the sales factor.

For corporations:

- "New microbusiness" means an LLC that on or after January 1, 2017, is organized under the laws of this state or has qualified to transact intrastate business in this state and has first commenced doing business in this state on or after the time of its organization. In determining whether the taxpayer has first commenced doing business in the state during the taxable year, the provisions of subdivision (f) of Section 17276 would apply except that "new microbusiness" would be substituted for "new business."

For LLC, LLP, and LPs:

- "New microbusiness" means an LLC, LLP, or LP that on or after January 1, 2017, is organized under the laws of this state or has qualified to transact intrastate business in this state and has first commenced doing business in this state on or after the time of its organization. In determining whether the taxpayer has first commenced doing business in the state during the taxable year, the provisions of subdivision (f) of Section 17276 shall apply except that "new microbusiness" shall be substituted for "new business."

Gross receipts derived from or attributable to this state of any other business, in whatever form conducted, that is owned directly or indirectly by persons that are treated as related to the new microbusiness, would be aggregated with the gross receipts derived from or attributable to the state of the new microbusiness to determine whether the new microbusiness qualifies for the reduced annual tax under this bill.

TECHNICAL CONSIDERATIONS

To correct cross referencing errors, the following amendments are recommended:

On page 13, line 30, strike "limited liability company" and insert "corporation"

On page 13, line 36, strike (f) and insert, (g)

On page 13, line 36, strike "17276" and insert "24416"

FISCAL IMPACT

Department costs have yet to be determined. As the bill continues to move through the legislative process, costs will be identified and a budget change proposal may be pursued if necessary.

ECONOMIC IMPACT

This bill would result in the following revenue loss:

Estimated Revenue Impact of AB 2625 As Amended May 2, 2016 Assumed Enactment After June 30, 2016 ($ in Millions)		
2016-17	2017-18	2018-19
-$13	-$55	-$110

This analysis does not account for changes in employment, personal income, or gross state product that could result from this bill.

Revenue Discussion

Based on new business registration data from the Secretary of State (SOS) and data from the department for years 2009-2015, it is estimated that in 2017 approximately 88,000 corporations, and 45,000 new LLCs, LLPs, and LPs would register and be doing business per the limitations specified in the bill.

The estimated revenue loss for 2017 does not include corporations because they are not subject to minimum franchise tax in their first year of operation. However, approximately 45,000 LLCs, LPs, and LLPs would be subject to the annual tax and benefit from the reduced tax in tax year 2017, resulting in an estimated revenue loss of $22 million. For the 2018 tax year, it is estimated that 80,000 first and second year LLCs, LPs, and LLPs and 70,000 second year corporations would benefit from reduced minimum franchise and annual tax for a total estimated revenue loss of $90 million. The revenue loss would be phased in over a five year period, reaching $230 million in 2021 and would continue to increase with the establishment of new microbusinesses in California.

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

SUPPORT/OPPOSITION[1]

Support: Cal Small Business.

Opposition: California Tax Reform Association.

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[1] As provided by the staffer.