DEPARTMENT OF FINANCE BILL ANALYSIS

AMENDMENT DATE: February 11, 2009
POSITION: Oppose

BILL NUMBER: SB 16
AUTHOR: A. Lowenthal
RELATED BILLS: Ch. 382/08 (SB 585)

BILL SUMMARY: Low-Income Housing Tax Credits

This bill, as an urgency measure, would 1) make the Low-Income Housing Credit (LIHC) refundable and 2) extend partnership allocation rules, as specified.

FISCAL SUMMARY

The Franchise Tax Board (FTB) estimates that this bill would create revenue losses of $200,000 in 2011-12, $1.8 million in 2012-13, $6.3 million in 2013-14, $11.0 million in 2014-15, $9.0 million in 2015-16, and $1.7 million in 2016-17. The FTB also notes that over an eight-year period beginning with fiscal year 2012-13 and ending 2019-20, the revenue impact of this bill would be neutral as aggregate credit usage over this period would simply be pushed into earlier fiscal years.

The FTB estimates that this bill would create a one-time implementation cost of $521,000 and ongoing annual costs of $14,000 both beginning in fiscal year 2011-12.

COMMENTS

The Department of Finance is opposed to this bill for the following reasons:

- Although the revenue impact from allowing the LIHC to be refundable would be revenue neutral over time, the state would lose the use of funds in the range of $2 million to $10 million annually from 2012-13 through 2016-17. Offsetting gains from fewer credits claimed in later years would not occur until 2017-18.
- Providing a refundable credit would result in a direct government outlay and would set a precedence for making other credits refundable to help taxpayers who are having financial difficulties during this economic downturn.
- It is questionable whether using the tax system to fund what is in essence a grant program is the most efficient way of increasing investment in low-income housing projects. If additional state support is deemed appropriate for encouraging construction of low-income housing, it may be prudent to consider using existing expenditure programs under Housing and Community Development or the California Housing Finance Agency to meet the need. This would allow the amount spent to be strictly limited and would require that the expenditure be reviewed annually to ensure it continues to be the highest priority use of the funds.
- This bill creates implementation costs that the FTB would be unable to absorb.
- The FTB is concerned that this bill could increase the likelihood of refundable credit fraud.
- This bill would set a precedent for business tax credits by allowing the LIHC to be refundable under corporation tax law.

Analyst/Principal	Date	Program Budget Manager	Date
(0723) C. Angaretis		Mark Hill	

Department Deputy Director — Date

Governor's Office: By: Date: Position Approved_______
Position Disapproved

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ANALYSIS

A. Programmatic Analysis

This bill would take effect immediately as an urgency measure.

1) Making the LIHC refundable.

Under existing federal and state law, LIHCs are non-refundable. The California Tax Credit Allocation Committee (CTCAC) allocates the LIHC to the taxpayer. This credit is applied against liability and any remaining credit is carried forward to reduce future year tax liabilities.

This bill would allow the LIHC to be refundable for projects that have or will receive a preliminary reservation on or after July 1, 2008, and before January 1, 2011, unless a financial closing, as specified, has occurred prior to the bill's effective date.

After applying the credit to reduce taxes owed, the excess amount would be refundable. The refunds would be made after all tax liabilities, including, tax, penalties, interest, and fees, have been paid. The refundable amounts determined by FTB would be transferred from the Personal Income Tax Fund or Corporation Income Tax Fund to the Tax Relief and Refund Account. These funds are General Fund accounts.

In addition, this bill would specify that any credit refunded to the taxpayer would not be included in income subject to tax.

2) Extending partnership allocation rules.

Current federal law allows a LIHC for the costs of constructing, rehabilitating, or acquiring low-income housing and is claimed over ten years. The CTCAC has the authority to oversee the process and allocate the federal and state credit.

Current state law conforms to federal law with respect to the LIHC, except that the state LIHC is claimed over four years, is limited to projects located in California, and is allocated in amounts equal to the sum of the following:

- For calendar year 2009, the amount of LIHC available is $85 million.
- The unused housing credit ceiling, if any, for the preceding year.
- The amount of housing credit ceiling returned in the current calendar year.

Current federal law requires a partner's distributive share of income, gain, loss, deduction, or credit to be determined in accordance with the partner's interest in the partnership by taking into account all facts and circumstances if one of the following occurs:

- The partnership agreement does not provide as to the partner's distributive share of income, gain, loss, deduction, or credit; or
- The allocation of income, gain, loss, deduction or credit to a partner under the partnership agreement does not have substantial economic effect.

Chapter 382, Statutes of 2008 (SB 585) allows partnership allocations on LIHC projects that receive preliminary reservations between January 1, 2009 through January 1, 2016, to be based on a partnership agreement regardless of how the federal LIHC is allocated or where the allocation under the terms of the agreement has substantial economic effect.

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Any loss or deduction from the sale or disposition of a partnership interest where the LIHC was allocated without substantial economic effect is required to be deferred until the first taxable year immediately following the end of the ten-year credit period for which the federal credit is allowed.

This bill would extend the special partnership allocation by agreement rule retroactively to projects that receive a preliminary reservation during calendar year 2008.

Discussion:

According to a background sheet provided by the author's office, the stated purpose of this bill is as follows:

"SB 16 will provide an immediate economic stimulus by keeping ready-to-go housing developments on track and will increase private investment in affordable housing at no net cost to the state."

B. Fiscal Analysis

The FTB estimates revenue losses of $200,000 in 2011-12, $1.8 million in 2012-13, $6.3 million in 2013-14, $11 million in 2014-15, $9.0 million in 2015-16, and $1.7 million in 2016-17. The FTB also notes that over an eight year period beginning with fiscal year 2012-13 and ending 2019-20, the revenue impact of this bill would be neutral as aggregate credit usage over this period would simply be pushed into earlier fiscal years.

The FTB estimates that this bill would create a one-time implementation cost of $521,000 in large part because this would be the first time they have administered a refundable tax credit under Corporate Tax Law. The FTB also expects ongoing annual costs of $14,000. Both of these costs would begin in fiscal year 2011-12.

Code/Department Agency or Revenue Type	SO LA CO RV	PROP 98	FC	2008-2009	FC	2009-2010	FC	2010-2011	Fund Code
		(Fiscal Impact by Fiscal Year) (Dollars in Thousands)							
1730/FTB	SO	No		-------------------- See Fiscal Analysis ---------------------					0001
1147/Pers Inc Tax	RV	No		-------------------- See Fiscal Analysis ---------------------					0001
1104/Corp Tax	RV	No		-------------------- See Fiscal Analysis ---------------------					0001