



**STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE ENROLLED BILL ANALYSIS**

DRAFT

Date Amended:	Enrolled	Bill No:	AB 2831
Tax:	Tax on Insurers	Author:	Ridley-Thomas
Related Bills:			

BILL SUMMARY

Among other things, this bill would extend until January 1, 2012, for calendar years 2007 through 2011, the operation of the insurance tax credit for insurers that invest in a community development financial institution (CDFI) that lends to underserved, low-income urban, rural, or reservation-based communities in this state, which is due to expire on January 1, 2007.¹

ANALYSIS

Current Law

Section 12201 of the Revenue and Taxation Code (Section) imposes an annual tax on all insurers doing business in this state. For insurers other than title insurers and ocean marine insurers, Section 12221 specifies that the basis of the annual tax is gross premiums, less return premiums, received by the insurer on business done in this state. For insurers transacting title insurance, Section 12231 specifies that the basis of the annual tax is all income from business done in this state except interest and dividends, rents from real property, profits from the sale of investments, and income from investments. For insurers transacting ocean marine insurance, Section 12101 provides that the annual tax is measured by that portion of the underwriting profit of the insurer from the ocean marine insurance written in the United States, of which the gross premiums from ocean marine insurance written in this state bear to the gross premiums from ocean marine insurance written within the United States, at the rate of 5 percent.

Section 12202 sets the current rate of the annual tax at 2.35 percent, except for specified premiums that are taxed at 0.50 percent. Under Section 12204, the tax imposed on insurers is in lieu of all other state, county, and municipal taxes and licenses, including income taxes, with specified exceptions.

Section 12209 allows as a credit against the amount of insurance tax an amount equal to 20 percent of the amount of each qualified investment made by an insurer during the year into a CDFI. A CDFI is defined as a private financial institution located in California and certified by the Department of Insurance (DOI), California Organized Investment Network (COIN), whose primary mission is community development and which lends in underserved, low-income urban, rural, or reservation based communities in California. A CDFI may include a community development bank, a community development loan fund, a community development credit union, a micro-enterprise fund, community development corporation-based lenders, and venture funds.

¹ Please refer to Comment 4, below, regarding the sunset date for this credit.

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Under Section 12209, a qualified investment is an investment in a CDFI that is:

- 1) a deposit or loan that does not earn interest;
- 2) an equity investment; or
- 3) an equity-like debt instrument that conforms to the specifications for these instruments as prescribed by the U.S. Department of the Treasury CDFI Fund, or its successor.

All qualified investments must be equal to or greater than \$50,000 and made for a minimum of sixty (60) months to qualify for a 20 percent tax credit during the year in which the investment was made. These tax credits are also available under the Personal Income and Bank and Corporation Tax Law. The combined amount of qualified investments available under these three tax laws is limited to a total amount of \$10 million per year for a total annual tax credit limit of \$2 million per year (\$10 million X 20%).

COIN administers the CDFI program by certifying and issuing certificates to CDFIs that wish to receive qualified investments and by certifying the tax credits for investors. COIN is also required to provide the Board of Equalization with an annual list of the names and taxpayers' California identification numbers for every taxpayer making a withdrawal or partial withdrawal of a qualified investment before the expiration of 60 months from the date of the qualified investment.

The CDFI program will remain in effect only until January 1, 2007, covering the taxable calendar years through 2006, and Section 12209 will be repealed as of December 31, 2007.

Proposed Law

This bill would amend Section 12209 to extend until January 1, 2012, the operation of the insurance tax credit for insurers that invest in a CDFI that lends to underserved, low-income urban, rural, or reservation-based communities in this state. This bill would also make the following additional amendments to Section 12209:

- Provide that the COIN is required to evaluate, in addition to accept, applications for certifying CDFIs;
- Provide that the Insurance Commissioner may develop instructions, procedures, and standards for applications, and for administering the criteria for the evaluation of CDFI applications;
- Provide that a CDFI certificate may be issued for a specified period of time, and may include reasonable conditions to effectuate the intent of this section; and,
- Provide that the Insurance Commissioner may revoke or suspend a certification, if the commissioner finds that a CDFI no longer meets the requirement for certification.

Additionally, this bill would add Article 1.1 (commencing with Section 12939) to Division 3 of Chapter 2 of the Insurance Code to establish the California Community Development Financial Institution Tax Credit Program (CDFI tax credit program), and would, among other things, provide the following Legislative findings and declarations:

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- CDFIs strive to bridge the growing gap that exists between the financial products and services available to the economic mainstream and those offered to low-income people and communities.
- CDFIs serve a critical role in addressing issues of poverty and access to credit in economically disadvantaged communities by providing services such as consumer credit counseling, financial literacy training, homeownership counseling, and technical assistance to small business owners.
- It is the intent of the Legislature to provide an incentive in the form of California tax credits to attract much needed additional private capital investments that would not otherwise be available to CDFIs without the benefit of such an incentive.

The CDFI tax credit program would also require: 1) CDFIs receiving insurance tax credit investments to submit reports to the DOI and COIN on their use of the program; and 2) the DOI and COIN to biennially include in the report required by Insurance Code Section 12922 information on the CDFI tax credit program based on the reports submitted by the CDFIs.

This bill would require the Legislative Analyst's Office to prepare an analysis by December 31, 2010, based upon data provided by the Franchise Tax Board, the DOI, and COIN, on the CDFI tax credits' fiscal impact and the resulting benefits from the use of the CDFI tax credit investments by economically disadvantaged communities and low income people in California.

Background

The current insurance tax credit for insurers that invest in a CDFI that lends to underserved, low-income urban, rural, or reservation-based communities in this state was created in 1999 by Assembly Bill 145 (Ch. 821, Vincent), which provided for a three-year, 20 percent tax credit for qualified deposits of \$50,000 or more. The credit was extended in 2001 by Senate Bill 409 (Ch. 535, Vincent) until January 1, 2007. SB 409 also expanded and clarified the definition of qualified investments, and provided for a carry-over of any unused tax credits to future years.

COMMENTS

1. **Sponsor and purpose.** This bill is sponsored by the DOI and is primarily intended to extend the current credit for investments in CDFIs until January 1, 2017. According to the sponsor, this bill is also intended to: 1) increase the combined annual limit for qualified investments from \$10 million to \$25 million; 2) make changes to the certification process for CDFIs and investors; and 3) authorize the Insurance Commissioner to develop instructions, procedures, standards, and regulations to administer the CDFI Tax Certification Program (Program). According to the sponsor, the Program has become well-known and established with both CDFIs and investors such that the demand far exceeds the supply of tax credits. According to the sponsor, there are now 78 certified CDFIs in California. This represents a 66 percent increase from the 47 that were certified when SB 409 was enacted in 2001 to extend the program until January 1, 2007.

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According to the sponsor, in calendar year 2005, the Program was so popular with investors and CDFIs that the entire annual amount available for tax credits was exhausted by 11 proposals received in January 2005. In 2006, four investments were received on the first business day of the calendar year that represented 80 percent of the total annual amount available.

In addition, according to the DOI staff, this bill would put in place mechanisms to encourage a broad distribution and equitable access to the Program by both small and large participants. It would also provide a set aside to encourage the insurance industry to participate in community development investing, given that they do not enjoy the same incentives as other financial institutions, such as banks.

2. **Key Amendments. The August 22, 2006 amendments** clarified that the LAO's analysis of the fiscal impact of the CDFI tax credits be based upon data provided by the Franchise Tax Board, the DOI, and COIN, and that these agencies are to provide such data to the LAO by September 30, 2010. **The August 9, 2006 amendments** made the following changes to the LAO analysis: 1) changed the due date of the analysis from June 30, 2011, to December 31, 2010; and 2) specified that the analysis include the CDFI tax credits' fiscal impact and the resulting benefits from the use of the CDFI tax credit investments by economically disadvantaged communities and low income people in California. **The August 7, 2006 amendments** changed the repeal date of the CDFI tax credits from January 1, 2017, to January 1, 2012. The amendments also require the LAO to prepare an analysis of the CDFI tax credits' fiscal impact and effect on business activity and employment by June 30, 2011. **The June 21, 2006 amendments** made technical nonsubstantive changes. **The June 15, 2006 amendments** added back the provision regarding setting a limit on the amount of total qualified investments in any calendar year made by a single CDFI to the lesser of either \$10 million, 40 percent of the authorized annual aggregate qualified investments, or an amount determined by the Insurance Commissioner. **The May 26 amendments** delete the previously proposed amendment that increased the maximum aggregate amount of qualified investments made by all taxpayers for each calendar year to \$25 million and restore the \$10 million maximum aggregate amount of qualified investments permitted under current law; and 2) delete the previously proposed provisions that would have limited the amount of total qualified investments made by a single CDFI. **The May 17 amendments** added an article heading and required reports to be submitted to the DOI and COIN. These amendments did not impact the Board.
3. **The Board staff does not foresee any administrative problems with this bill.** The Board of Equalization, the State Controller, and the DOI share administrative responsibility for the insurance tax program. Section 28 of Article XIII of the California Constitution states that the Board shall assess taxes under the Insurance Tax Law. Upon recommendation from the DOI, the Board also issues deficiency assessments in cases of underpayment of the tax by an insurer. The Office of the Controller is responsible for collecting the tax and issuing refunds. Audit verification work is the responsibility of the DOI.

As the law is currently administered, the DOI would be responsible for the verification of the tax credit. It is anticipated that the extension of the tax credit as

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proposed by this bill would have a minimal impact on the Board's current functions under the Insurance Tax Law.

4. **Technical correction.** Subdivision (k) of Section 12209 provides for a sunset date of December 31, 2017. However, subdivision (a) of Section 12209 provides that the credit is allowed for each year beginning January 1, 1999, and ending before January 1, 2017, which would be for the taxable years 1999 through 2016. Board staff believes that the sunset date in subdivision (k) should be changed to January 1, 2017, to include only the calendar year 2016 for consistency with subdivision (a). Board staff believes that this correction alleviates any confusion that could arise from whether the credit would apply to taxable year 2017 because subdivision (k) provides for a sunset date of December 31, 2017.
5. **Suggested definition.** In order to simplify the language of Section 12209, it is suggested that the term "COIN" be added as a defined term under subdivision (g) of Section 12209 as: (3) "COIN" means the Department of Insurance, California Organized Investment Network, or any successor thereof. It is further suggested that each mention of "Department of Insurance, California Organized Investment Network, [or any successor thereof] [or its successor]" be replaced by "COIN." The term "COIN" has already been used in subdivision (d)(5).

It is also suggested that the same definition be added to Section 17053.57, subdivision (f), and Section 23657, subdivision (f), and that the same term replacements be made in these sections.

COST ESTIMATE

The Board's administrative costs related to this bill would be insignificant (i.e., under \$10,000).

REVENUE ESTIMATE

This bill would extend until January 1, 2012, the operation of the insurance tax credit for insurers that invest in a CDFI that lends to urban, rural, or reservation-based communities in this state. This bill would maintain the current \$2 million annual limit for the allocated tax credit. Accordingly, this bill could potentially decrease the General Fund by \$10 million from calendar years 2007 through 2011, inclusive.

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