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April 7, 2010

TO: Members
Joint Committee on Finance

FROM: Bob Lang, Director

SUBJECT: Assembly Bill 756: Individual Income and Corporate Income and Franchise Taxes -- Dairy Farm Investment Tax Credit

Assembly Bill 756, which would extend the dairy farm investment tax credit, under the state individual income and corporate income and franchise taxes, was introduced on February 17, 2010, and referred to the Assembly Committee on Agriculture. Assembly Amendment 1 was offered on February 25, and adopted on March 2, 2010, by a vote of 11 to 0. AB 756 as amended, was recommended for passage by a vote of 11 to 0, on March 2. The bill was then referred to the Joint Committee on Finance.

CURRENT LAW

Under current law, a tax credit may be claimed, for tax years that begin after December 31, 2003, and before January 1, 2010, equal to 10% of the amount paid by the claimant during the tax year for dairy farm modernization or expansion related to the operation of the claimant's dairy farm.

"Dairy farm modernization or expansion" is defined as the construction, improvement, or acquisition of buildings or facilities, or the acquisition of equipment for dairy animal housing, confinement, animal feeding, milk production, or waste management, including the following, if used exclusively related to dairy animals and if acquired and placed in service in the state during tax years that begin after December 31, 2003, and before January 1, 2010: (a) freestall barns; (b) fences; (c) watering facilities; (d) feed storage and handling equipment; (e) milking parlors; (f) robotic equipment; (g) scales; (h) milk storage and cooling facilities; (i) bulk tanks; (j) manure pumping and storage facilities; (k) digesters; and (l) equipment used to produce energy. "Dairy animals" include heifers raised as replacement dairy animals. "Dairy farm" includes a facility used to raise heifers as replacement to dairy animals.

"Used exclusively" means used to the exclusion of all other uses except for use not exceeding 5% of total use.

The aggregate amount of dairy and livestock modernization tax credits that may be claimed by a taxpayer is $50,000. The credits cannot be claimed for any amounts also claimed as business expense deductions. Unused credit amounts can be carried forward up to 15 years to offset future tax liabilities.

Partnerships, limited liability companies (LLCs), and S corporations cannot claim a tax credit, but eligibility for, and the amount of credit is based on each entity's payment of eligible expenses, but cannot exceed the aggregate tax credit limit of $50,000. A partnership, LLC, or tax-option corporation is required to compute the amount of credit that each of its partners, members, or shareholders may claim and provide that information to each of them. Partners, members of LLCs, and shareholders of tax-option corporations claim the credit in proportion to their ownership interest. If two or more persons own and operate a dairy or livestock farm, each person can claim the dairy or livestock tax credit in proportion to his or her ownership interest, subject to the $50,000 maximum limit on aggregate tax credit claims.

The table below, from Department of Revenue (DOR) aggregate individual income and corporate income and franchise tax statistics, shows the amount of dairy farm investment tax credits claimed and used to offset tax liabilities, for tax years 2004 through 2007. The amounts shown for available credits include unused credit carry-forwards from past years. The table shows that most of the credits available in a given year have not been used to offset current tax liabilities, but are available to be carried forward up to 15 years to offset future tax liabilities.

Dairy Farm Investment Tax Credits Tax Years 2004 - 2007

	2004	2005	2006	2007	Total
Credits Available*	$28,819,600	$41,994,800	$50,870,000	$61,485,000	$183,169,400
Count	6,744	8,796	9,777	10,549	
Credits Used	$13,184,000	$12,488,000	$8,677,900	$18,945,900	$53,295,800
Percent of Credits Available	45.75%	29.74%	17.06%	30.81%	29.10%
Count	6,643	6,675	6,261	8,445	
Percent of Total	98.50%	75.89%	64.04%	80.05%	

* Includes unused carryforwards

Source: Department of Revenue Aggregate Statistics

SUMMARY OF BILL

Assembly Bill 756 would extend the dairy farm investment tax credit by two years, so that a credit could be claimed for eligible investments made before January 1, 2012. Consequently, credits could be claimed for eligible investments in tax years 2010 and 2011. The bill would also increase the limit on aggregate credit claims from $50,000 to $75,000.

ASSEMBLY AMENDMENT 1

Assembly Amendment 1 specifies that the increase in the aggregate tax credit limit, from $50,000 to $75,000, would only apply to costs incurred after the effective date of the bill.

FISCAL EFFECT

Based on an analysis of the income and franchise tax returns of taxpayers who claimed the dairy farm investment tax credit for tax years 2004 through 2008, the Department of Revenue estimates that AB 756 would result in $25.6 million in additional tax credits being claimed in tax years 2010 and 2011. The bill would reduce state income and franchise tax revenues by an estimated $200,000 in 2010-11, and by $400,000 in 2011-12. DOR indicates that, because there have been large credit carry-forwards relative to new credit claims, it is estimated that much of the revenue reduction from extending the credit would be experienced over 10 years. Specifically, state income and franchise tax revenues would be reduced by an estimated $400,000 annually from 2011-12 through 2014-15, by $3.4 million in 2015-16, and by $12.0 million in 2016-17. The estimated fiscal effect would decrease to $6.7 million in 2019-20, and then to $750,000 in 2021-22, with no fiscal effect thereafter.

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