

AMENDED IN SENATE AUGUST 16, 2010
AMENDED IN SENATE AUGUST 5, 2010
AMENDED IN SENATE JUNE 16, 2010
AMENDED IN SENATE MAY 27, 2010
AMENDED IN ASSEMBLY JANUARY 25, 2010
AMENDED IN ASSEMBLY JANUARY 13, 2010
AMENDED IN ASSEMBLY JANUARY 6, 2010
AMENDED IN ASSEMBLY JANUARY 4, 2010

CALIFORNIA LEGISLATURE—2009–10 REGULAR SESSION

ASSEMBLY BILL

No. 1178

Introduced by Assembly Member Portantino

February 27, 2009

An act to amend Sections ~~17072, 17215, 17220, 19184, 19774, and 23701~~ of, to amend and repeal Sections ~~17131.4, 17131.5, 17215.1, and 17215.4~~ of, and to add Sections 17131.7, 17131.9, 17131.10, 17131.11, 17131.12, 17131.13, 17131.14, 17134.1, ~~17138.7~~, 17201.1, ~~17217, 17201.8~~, 17222.1, 24343.6, and 24345.1 to, the Revenue and Taxation Code, relating to taxation, to take effect immediately, tax levy.

LEGISLATIVE COUNSEL'S DIGEST

AB 1178, as amended, Portantino. Income taxes: federal conformity: Patient Protection and Affordable Care Act: Health Care and Education Reconciliation Act of ~~2010~~: ~~health savings accounts~~. *2010*.

The Personal Income Tax Law and the Corporation Tax Law, in specified conformity with federal income tax laws, provide certain gross

income exclusions, impose specified tax rates, and allow various deductions and credits in computing the income that is subject to the taxes imposed by those laws, as specified.

This bill would, under both laws, provide additional conformity with federal income tax laws by adopting specified provisions of the Patient Protection and Affordable Care Act and the Health Care and Education Reconciliation Act of 2010 relating to gross income exclusions for reimbursements for medical care expenses under specified plans for dependents, Indian health care benefits, free choice vouchers, participants in the National Health Service Corps, student loan repayments, adoption assistance, therapeutic discovery project credits, annual fees on branded prescriptions, unreimbursed medical expenses, hospital insurance tax, cafeteria plans, the economic substance doctrine and related penalties, and tax rates on distributions from a nonqualified medical savings accounts, as specified.

~~The Personal Income Tax Law authorizes various deductions in computing income that is subject to tax under that law.~~

~~This bill would allow a deduction in connection with health savings accounts in conformity with federal law for each taxable year beginning on or after January 1, 2013. In general, the deduction would be an amount equal to the aggregate amount paid in cash during the taxable year by, or on behalf of, an eligible individual, as defined, to a health savings account of that individual, as provided. This bill would also provide related conformity to that federal law for each taxable year beginning on or after January 1, 2013, with respect to treatment of the account as a tax-exempt trust, the allowance of rollovers from Archer Medical Savings Accounts, health flexible spending arrangements, or health reimbursement accounts to a health savings account, and penalties in connection therewith.~~

This bill would take effect immediately as a tax levy.

Vote: majority. Appropriation: no. Fiscal committee: yes.
State-mandated local program: no.

The people of the State of California do enact as follows:

- 1 ~~SECTION 1. Section 17072 of the Revenue and Taxation Code~~
- 2 ~~is amended to read:~~
- 3 ~~17072. (a) Section 62 of the Internal Revenue Code, relating~~
- 4 ~~to adjusted gross income defined, shall apply, except as otherwise~~
- 5 ~~provided.~~

1 ~~(b) Section 62(a)(2)(D) of the Internal Revenue Code, relating~~
2 ~~to certain expenses of elementary and secondary school teachers,~~
3 ~~shall not apply.~~

4 ~~(c) The deduction allowed by Section 17217 shall be allowed~~
5 ~~in computing adjusted gross income.~~

6 ~~(d) The amendments made to this section by the act adding this~~
7 ~~subdivision shall apply only to each taxable year beginning on or~~
8 ~~after January 1, 2013.~~

9 ~~SEC. 2. Section 17131.4 of the Revenue and Taxation Code~~
10 ~~is amended to read:~~

11 ~~17131.4. (a) Section 106(d) of the Internal Revenue Code,~~
12 ~~relating to contributions to health savings accounts, shall not apply.~~

13 ~~(b) This section shall apply to taxable years beginning on or~~
14 ~~after January 1, 2005, and before January 1, 2013.~~

15 ~~(c) This section shall remain in effect only until December 1,~~
16 ~~2013, and as of that date is repealed.~~

17 ~~SEC. 3. Section 17131.5 of the Revenue and Taxation Code~~
18 ~~is amended to read:~~

19 ~~17131.5. (a) Section 125(d)(2)(D) of the Internal Revenue~~
20 ~~Code, relating to the exception for health savings accounts, shall~~
21 ~~not apply.~~

22 ~~(b) This section shall apply to taxable years beginning on or~~
23 ~~after January 1, 2005, and before January 1, 2013.~~

24 ~~(c) This section shall remain in effect only until December 1,~~
25 ~~2013, and as of that date is repealed.~~

26 ~~SEC. 4.~~

27 ~~SECTION 1.~~ Section 17131.7 is added to the Revenue and
28 Taxation Code, to read:

29 17131.7. (a) Section 105(b) of the Internal Revenue Code,
30 relating to amounts expended for medical care, as amended by
31 Section 1004(d)(1) of the Health Care and Education Reconciliation
32 Act of 2010 (Public Law 111-152), shall apply, except as otherwise
33 provided.

34 (b) This section shall apply in the same manner and to the same
35 periods as the federal amendments referred to in subdivision (a)
36 apply for federal purposes, except as otherwise provided.

37 ~~SEC. 5.~~

38 ~~SEC. 2.~~ Section 17131.9 is added to the Revenue and Taxation
39 Code, to read:

1 17131.9. For taxable years beginning on or after January 1,
2 2011, Section 106(f) of the Internal Revenue Code, relating to
3 reimbursements for medicine restricted to prescribed drugs and
4 insulin, as added by Section 9003(c) of the Patient Protection and
5 Affordable Care Act (Public Law 111-148), shall apply, except as
6 otherwise provided.

7 ~~SEC. 6.~~

8 *SEC. 3.* Section 17131.10 is added to the Revenue and Taxation
9 Code, to read:

10 17131.10. (a) For taxable years beginning on or after January
11 1, 2014, Section 125(f) of the Internal Revenue Code, relating to
12 qualified benefits defined, as amended by Section 1515 of the
13 Patient Protection and Affordable Care Act (Public Law 111-148),
14 shall apply, except as otherwise provided.

15 (b) For taxable years beginning on or after January 1, 2013,
16 Section 125(i) of the Internal Revenue Code, relating to limitation
17 on health flexible spending arrangements, as added by Section
18 9005 of the Patient Protection and Affordable Care Act (Public
19 Law 111-148) and amended by Section 10902 of the Patient
20 Protection and Affordable Care Act (Public Law 111-148) and
21 Section 1403 of the Health Care and Education Reconciliation Act
22 of 2010 (Public Law 111-152), shall apply, except as otherwise
23 provided.

24 (c) For taxable years beginning on or after January 1, 2011,
25 Section 125(j) of the Internal Revenue Code, relating to simple
26 cafeteria plans for small businesses, as added by Section 9022 of
27 the Patient Protection and Affordable Care Act (Public Law
28 111-148), shall apply, except as otherwise provided.

29 ~~SEC. 7.~~

30 *SEC. 4.* Section 17131.11 is added to the Revenue and
31 Taxation Code, to read:

32 17131.11. For taxable years beginning on or after January 1,
33 2010, Section 137 of the Internal Revenue Code, relating to
34 adoption assistance programs, as amended by Section 10909(a)(2)
35 of the Patient Protection and Affordable Care Act (Public Law
36 111-148), shall apply, except as otherwise provided.

37 ~~SEC. 8.~~

38 *SEC. 5.* Section 17131.12 is added to the Revenue and Taxation
39 Code, to read:

17131.12. (a) Section 139D of the Internal Revenue Code, relating to Indian health care benefits, as added by Section 9021 of the Patient Protection and Affordable Care Act (Public Law 111-148), shall apply, except as otherwise provided.

(b) This section shall apply to benefits and coverage provided after March 23, 2010.

(c) No inference shall be made with respect to the enactment the act adding this section with respect to the exclusion from gross income of benefits provided by either an Indian tribe or tribal organization that are not within the scope of this section or were provided prior to March 23, 2010.

~~SEC. 9.~~

SEC. 6. Section 17131.13 is added to the Revenue and Taxation Code, to read:

17131.13. For taxable years beginning on or after January 1, 2014, Section 139D of the Internal Revenue Code, relating to free choice vouchers, as added by Section 10108(f) of the Patient Protection and Affordable Care Act (Public Law 111-148), shall apply, except as otherwise provided.

~~SEC. 10.~~

SEC. 7. Section 17131.14 is added to the Revenue and Taxation Code, to read:

17131.14. (a) Any grant made in any year by the Secretary of the Treasury under Section 9023(e) of the Patient Protection and Affordable Care Act (Public Law 111-148), to a person that places in service qualified therapeutic discovery project property, shall not be includable in the gross income or the alternative minimum taxable income of the taxpayer.

(b) This section shall apply in the same manner and to the same periods as the provisions of federal law referred to in subdivision (a) apply for federal purposes, except as otherwise provided.

~~SEC. 11.~~

SEC. 8. Section 17134.1 is added to the Revenue and Taxation Code, to read:

17134.1. For taxable years beginning on or after January 1, 2010, Section 108(f)(4) of the Internal Revenue Code, relating to payments under the National Health Service Corps loan repayment program and certain state loan repayment programs, as amended by Section 10908 of the Patient Protection and Affordable Care

1 Act (Public Law 111-148), shall apply, except as otherwise
2 provided.

3 ~~SEC. 12. Section 17138.7 is added to the Revenue and Taxation~~
4 ~~Code, to read:~~

5 ~~17138.7. For each taxable year beginning on or after January~~
6 ~~1, 2013, Section 106 of the Internal Revenue Code, as amended~~
7 ~~by Section 302 of the Tax Relief and Health Care Act of 2006~~
8 ~~(Public Law 109-432), relating to health savings accounts, shall~~
9 ~~apply, except as otherwise provided.~~

10 ~~SEC. 13.~~

11 ~~SEC. 9.~~ Section 17201.1 is added to the Revenue and Taxation
12 Code, to read:

13 17201.1. (a) Section 162(l)(1) of the Internal Revenue Code,
14 relating to allowance of deduction, as amended by Section
15 1004(d)(2) of the Health Care and Education Reconciliation Act
16 of 2010 (Public Law 111-152), shall apply, except as otherwise
17 provided.

18 (b) Section 162(l)(2)(B) of the Internal Revenue Code, relating
19 to other coverage, as amended by Section 1004(d)(3) of the Health
20 Care and Education Reconciliation Act of 2010 (Public Law
21 111-152), shall apply, except as otherwise provided.

22 (c) This section shall apply in the same manner and to the same
23 periods as the federal amendments referred to in subdivision (a)
24 or subdivision (b), respectively, apply for federal purposes, except
25 as otherwise provided.

26 ~~SEC. 14. Section 17201.8 is added to the Revenue and Taxation~~
27 ~~Code, to read:~~

28 ~~17201.8. For taxable years beginning on or after January 1,~~
29 ~~2013, Section 213 of the Internal Revenue Code, relating to~~
30 ~~medical, dental, etc., expenses, as amended by Section 9013 of~~
31 ~~the Patient Protection and Affordable Care Act (Public Law~~
32 ~~111-148), shall apply, except as otherwise provided.~~

33 ~~SEC. 15.~~

34 ~~SEC. 10.~~ Section 17215 of the Revenue and Taxation Code is
35 amended to read:

36 17215. (a) Section 220(a) of the Internal Revenue Code,
37 relating to deduction allowed, is modified to provide that the
38 amount allowed as a deduction shall be an amount equal to the
39 amount allowed to that individual as a deduction under Section
40 220 of the Internal Revenue Code, relating to medical savings

1 accounts, on the federal income tax return filed for the same taxable
2 year by that individual.

3 (b) For taxable years beginning on or after January 1, 2011,
4 Section 220(d)(2)(A) of the Internal Revenue Code, as amended
5 by Section 9003(b) of the Patient Protection and Affordable Care
6 Act (Public Law 111-148), shall apply, except as otherwise
7 provided.

8 (c) Section 220(f)(4) of the Internal Revenue Code, relating to
9 additional tax on distributions not used for qualified medical
10 expenses, is modified by substituting “10 percent” for “15 percent.”

11 (d) For taxable years beginning on or after January 1, 2011,
12 Section 220(f)(4) of the Internal Revenue Code, relating to
13 additional tax on distributions not used for qualified medical
14 expenses, as amended by Section 9004 of the Patient Protection
15 and Affordable Care Act (Public Law 111-148), is modified by
16 substituting “12.5 percent” for “20 percent.”

17 ~~SEC. 16. Section 17215.1 of the Revenue and Taxation Code~~
18 ~~is amended to read:~~

19 ~~17215.1. (a) Section 220(f)(5) of the Internal Revenue Code,~~
20 ~~relating to rollover contributions, shall not apply.~~

21 ~~(b) This section shall apply to taxable years beginning on or~~
22 ~~after January 1, 2005, and before January 1, 2013.~~

23 ~~(c) This section shall remain in effect only until December 1,~~
24 ~~2013, and as of that date is repealed.~~

25 ~~SEC. 17. Section 17215.4 of the Revenue and Taxation Code~~
26 ~~is amended to read:~~

27 ~~17215.4. (a) Section 223 of the Internal Revenue Code, relating~~
28 ~~to health savings accounts, shall not apply.~~

29 ~~(b) This section shall apply to taxable years beginning on or~~
30 ~~after January 1, 2005, and before January 1, 2013.~~

31 ~~(c) This section shall remain in effect only until December 1,~~
32 ~~2013, and as of that date is repealed.~~

33 ~~SEC. 18. Section 17217 is added to the Revenue and Taxation~~
34 ~~Code, to read:~~

35 ~~17217. For each taxable year beginning on or after January 1,~~
36 ~~2013, all of the following shall apply:~~

37 ~~(a) Section 223 of the Internal Revenue Code, as amended by~~
38 ~~Section 404(c) of the Gulf Opportunity Zone Act of 2005 (Public~~
39 ~~Law 109-135), as amended by Title III of the Tax Relief and Health~~

1 Care Act of 2006 (Public Law 109-432), relating to health savings
2 accounts, shall apply, except as otherwise provided.

3 ~~(b) Section 223(e)(1) of the Internal Revenue Code shall be~~
4 ~~modified by substituting the phrase “Section 17651” for the phrase~~
5 ~~“section 511 (relating to imposition of tax of unrelated business~~
6 ~~income of charitable, etc., organizations),” contained therein.~~

7 ~~(c) Section 223(f)(4)(A) of the Internal Revenue Code shall be~~
8 ~~modified by substituting “2 ½ percent” for “10 percent,” contained~~
9 ~~therein.~~

10 ~~SEC. 19.~~

11 *SEC. 11.* Section 17220 of the Revenue and Taxation Code is
12 amended to read:

13 17220. (a) Section 164(a)(3) of the Internal Revenue Code,
14 relating to the deductibility of state, local, and foreign income, war
15 profits, and excess profits taxes, shall not apply.

16 (b) Section 164(b)(5) of the Internal Revenue Code, relating to
17 general sales taxes, shall not apply.

18 (c) In addition to the provisions of Section 164(c) of the Internal
19 Revenue Code, relating to deduction denied in case of certain
20 taxes, no deduction shall be allowed for any tax imposed under
21 Chapter 10.5 (commencing with Section 17935), Chapter 10.6
22 (commencing with Section 17941), or Chapter 10.7 (commencing
23 with Section 17951) of this part or under Part 11 (commencing
24 with Section 23001).

25 (d) For taxable years beginning on or after January 1, 2013,
26 Section 164(f) of the Internal Revenue Code, relating to deduction
27 for one-half of self-employment taxes, as amended by Sections
28 9015(b) and 10906(b) of the Patient Protection and Affordable
29 Care Act (Public Law 111-148), shall apply, except as otherwise
30 provided.

31 ~~SEC. 20.~~

32 *SEC. 12.* Section 17222.1 is added to the Revenue and Taxation
33 Code, to read:

34 17222.1. For taxable years beginning on or after January 1,
35 2011, no deduction shall be allowed for the fees imposed on
36 manufacturers or importers of branded prescription drugs by
37 Section 9008 of the Patient Protection and Affordable Care Act
38 (Public Law 111-148), as amended by Section 1404 of the Health
39 Care and Education Reconciliation Act of 2010 (Public Law
40 111-152).

1 ~~SEC. 21. Section 19184 of the Revenue and Taxation Code is~~
2 ~~amended to read:~~

3 ~~19184. (a) A penalty of fifty dollars (\$50) shall be imposed~~
4 ~~for each failure, unless it is shown that the failure is due to~~
5 ~~reasonable cause, by any person required to file who fails to file~~
6 ~~a report at the time and in the manner required by any of the~~
7 ~~following provisions:~~

8 ~~(1) Subdivision (c) of Section 17507.~~

9 ~~(2) Section 220(h) of the Internal Revenue Code, relating to~~
10 ~~medical savings accounts for taxable years beginning on or after~~
11 ~~January 1, 1997.~~

12 ~~(3) Section 223(h) of the Internal Revenue Code.~~

13 ~~(4) Subdivision (b) of Section 17140.3 or subdivision (b) of~~
14 ~~Section 23711.~~

15 ~~(5) Subdivision (e) of Section 23712.~~

16 ~~(b) (1) Any individual who satisfies both of the following~~
17 ~~conditions:~~

18 ~~(A) Is required to furnish information under Section 17508 as~~
19 ~~to the amount designated nondeductible contributions made for~~
20 ~~any taxable year.~~

21 ~~(B) Overstates the amount of those contributions made for that~~
22 ~~taxable year, shall pay a penalty of one hundred dollars (\$100) for~~
23 ~~each overstatement unless it is shown that the overstatement is due~~
24 ~~to reasonable cause.~~

25 ~~(2) Any individual who fails to file a form required to be filed~~
26 ~~by the Franchise Tax Board under Section 17508 shall pay a~~
27 ~~penalty of fifty dollars (\$50) for each failure unless it is shown~~
28 ~~that the failure is due to reasonable cause.~~

29 ~~(c) Article 3 (commencing with Section 19031) of this chapter~~
30 ~~(relating to deficiency assessments) shall not apply in respect of~~
31 ~~the assessment or collection of any penalty imposed under this~~
32 ~~section.~~

33 ~~(d) The amendments made to this section by the act adding this~~
34 ~~subdivision shall apply only to each taxable year beginning on or~~
35 ~~after January 1, 2013.~~

36 ~~SEC. 22.~~

37 ~~SEC. 13. Section 19774 of the Revenue and Taxation Code is~~
38 ~~amended to read:~~

39 ~~19774. (a) If a taxpayer has a noneconomic substance~~
40 ~~transaction understatement for any taxable year, there shall be~~

1 added to the tax an amount equal to 40 percent of the amount of
2 that understatement.

3 (b) (1) Subdivision (a) shall be applied by substituting “20
4 percent” for “40 percent” with respect to the portion of any
5 noneconomic substance transaction understatement with respect
6 to which the relevant facts affecting the tax treatment of the item
7 are adequately disclosed in the return or a statement attached to
8 the return.

9 (2) For taxable years beginning before January 1, 2003,
10 “adequately disclosed” includes the disclosure of the tax shelter
11 identification number on the taxpayer’s return as required by
12 subdivision (c) of Section 18628, as applicable for the year in
13 which the transaction was entered into.

14 (c) For purposes of this section:

15 (1) The term “noneconomic substance transaction
16 understatement” means any amount which would be an
17 understatement under Section 6662A(b) of the Internal Revenue
18 Code, as modified by subdivision (b) of Section 19164.5 if Section
19 6662A(b) of the Internal Revenue Code were applied by taking
20 into account items attributable to noneconomic substance
21 transactions rather than items to which Section 6662A(b) applies.

22 (2) A “noneconomic substance transaction” includes:

23 (A) The disallowance of any loss, deduction or credit, or addition
24 to income attributable to a determination that the disallowance or
25 addition is attributable to a transaction or arrangement that lacks
26 economic substance including a transaction or arrangement in
27 which an entity is disregarded as lacking economic substance. A
28 transaction shall be treated as lacking economic substance if the
29 taxpayer does not have a valid nontax California business purpose
30 for entering into the transaction.

31 (B) Any disallowance of claimed tax benefits by reason of a
32 transaction lacking economic substance, within the meaning of
33 Section 7701(o) of the Internal Revenue Code, relating to
34 clarification of economic substance doctrine, as added by Section
35 1409(a) of the Health Care and Education Reconciliation Act of
36 2010 (Public Law 111-152), except as otherwise provided.

37 (i) For purposes of this subparagraph, the phrase “apart from
38 state income tax effects” shall be substituted for the phrase “apart
39 from federal income tax effects” in each place it appears in Section
40 7701(o)(1) of the Internal Revenue Code.

(ii) For purposes of this subparagraph, the phrase “any federal or local income tax effect which is related to a state income tax effect shall be treated in the same manner as a state income tax effect” is substituted for the phrase “any state or local income tax effect which is related to a Federal income tax effect shall be treated in the same manner as a Federal income tax effect” in Section 7701(o)(3) of the Internal Revenue Code.

(d) (1) If the notice of proposed assessment of additional tax has been sent with respect to a penalty to which this section applies, only the Chief Counsel of the Franchise Tax Board may compromise all or any portion of that penalty.

(2) The exercise of authority under paragraph (1) shall be at the sole discretion of the Chief Counsel of the Franchise Tax Board and may not be delegated.

(3) Notwithstanding any other law or rule of law, any determination under this subdivision may not be reviewed in any administrative or judicial proceeding.

(e) Notwithstanding anything to the contrary in this section, if a penalty has been assessed for federal income tax purposes pursuant to Section 6662(b)(6) of the Internal Revenue Code, as added by Section 1409(a) of the Health Care and Education Reconciliation Act of 2010 (Public Law 111-152), on an underpayment attributable to the disallowance of claimed tax benefits by reason of a transaction lacking economic substance, then a penalty shall be imposed under this section for that portion of an understatement attributable to that transaction, and shall not be abated unless the taxpayer can establish that the imposition of the federal penalty under Section 6662 of the Internal Revenue Code for an underpayment attributable to that transaction was clearly erroneous.

(f) The amendments made to this section by the act adding this subdivision shall apply to notices mailed on or after the effective date of the act adding this subdivision.

~~SEC. 23.~~

SEC. 14. Section 23701i of the Revenue and Taxation Code is amended to read:

23701i. (a) A voluntary employees’ beneficiary association described in Section 501(c)(9) of the Internal Revenue Code, as amended by Section 1004(d)(4) of the Health Care and Education Reconciliation Act of 2010 (Public Law 111-152).

(b) The amendments made to this section by the act adding this subdivision shall apply in the same manner and to the same periods as the federal amendments referred to in subdivision (a) apply for federal purposes.

~~SEC. 24.~~

SEC. 15. Section 24343.6 is added to the Revenue and Taxation Code, to read:

24343.6. For taxable years beginning on or after January 1, 2014, Section 162(a) of the Internal Revenue Code, as amended by Section 10108(f) of the Patient Protection and Affordable Care Act (Public Law 111-148), shall apply, except as otherwise provided.

~~SEC. 25.~~

SEC. 16. Section 24345.1 is added to the Revenue and Taxation Code, to read:

24345.1. For taxable years beginning on or after January 1, 2011, no deduction shall be allowed for fees imposed on manufacturers or importers of branded prescription drugs by Section 9008 of the Patient Protection and Affordable Care Act (Public Law 111-148), as amended by Section 1404 of the Health Care and Education Reconciliation Act of 2010 (Public Law 111-152).

~~SEC. 26.~~

SEC. 17. This act provides for a tax levy within the meaning of Article IV of the Constitution and shall go into immediate effect.