

Date of Hearing: January 10, 2022

ASSEMBLY COMMITTEE ON REVENUE AND TAXATION

Autumn R. Burke, Chairwoman

AB 365 (O'Donnell) – As Amended January 3, 2022

Majority vote. Tax levy. Fiscal committee.

**SUBJECT:** Sales and use taxes: exemption: zero-emission and near-zero-emission drayage trucks

**SUMMARY:** Provides a partial sales tax exemption for "qualified drayage trucks". Specifically, **this bill:**

- 1) Contains the following legislative findings and declarations:
  - a) In 2020, the State Air Resources Board (CARB) adopted regulations to reduce greenhouse gas emissions from heavy-duty trucks and drayage trucks. These regulations include a first-in-the-world rule requiring truck manufacturers to transition from diesel trucks and vans to electric zero-emission trucks beginning in 2024 and requiring every new truck sold in California to be zero-emission by 2045. CARB approved the "Heavy-Duty Low NOx Omnibus Regulation," which requires manufacturers of heavy-duty diesel trucks to comply with tougher emission standards, overhaul engine testing procedures, and further extend engine warranties to ensure that emissions of oxides of nitrogen are reduced to help California meet federal air quality standards and critical public health goals;
  - b) Also in 2020, Governor Newsom issued Executive Order No. N-79-20, which, among other things, requires all drayage trucks in the state to be zero-emission by 2035 and sets a number of vehicle emissions goals for the state, including having 100% of heavy-duty vehicles in the state be zero-emission by 2045;
  - c) There are an estimated 30,000 drayage trucks that service California's ports each year. Most of these are used trucks. Used drayage trucks cost around \$50,000. New zero-emission trucks cost \$350,000. Unless funding is provided to offset the cost of new and used zero-emission trucks, it will be nearly impossible for individuals and small businesses to comply with the new requirement. If funding is [not] provided to offset the cost of new and used zero-emission trucks, the sales and use tax (SUT) will be too high for people to afford since it will be based on the full price of the truck;
  - d) Legislation is necessary to exclude zero-emission and near-zero-emission drayage trucks from the state portion of the SUT so individuals will be able to afford these new and used trucks to be in compliance with state mandates to meet the state's greenhouse gas emissions and public health goals;
  - e) The state currently exempts the following items from certain state SUTs:

- i) Zero-emission technology transit buses;
  - ii) Certain government purchases of public passenger transportation vehicles;
  - iii) Certain new or remanufactured trucks, truck tractors, semitrailers, or trailers that have an unladen weight of 6,000 pounds or more, or new or remanufactured trailer coaches or new or remanufactured auxiliary dollies, purchased from a dealer located outside this state for use without this state;
  - iv) Diesel fuel consumed during the activities of a farming business or food processing, as specified;
  - v) Farm equipment, machinery, and their parts sold to or purchased by specified persons engaged in the business of producing and harvesting agricultural products;
  - vi) Certain equipment used in manufacturing, research and development in biotechnology, and research and development in the physical, engineering, and life sciences; and,
  - vii) Electric power generation and distribution equipment when sold to or purchased by certain qualifying electric power generators or distributors for use primarily in electric power generation or production, or storage and distribution activities.
- 2) Provides, on and after January 1, 2023, a partial exemption under the SUT Law for gross receipts from the sale of a "qualified drayage truck".
  - 3) Defines a "qualified drayage truck" as a new or used drayage truck that meets, on or after January 1, 2021, the criteria of any of the following:
    - a) The California Hybrid and Zero-Emission Truck and Bus Voucher Incentive Project funded by the Air Quality Improvement Program established by Health and Safety Code Section 44274;
    - b) The Carl Moyer Memorial Air Quality Standards Attainment Program; or,
    - c) The Volkswagen Environmental Mitigation Trust for California.
  - 4) Provides that, notwithstanding any provision of the Bradley-Burns Uniform Local SUT Law or the Transactions and Use Tax Law, this bill's exemption shall not apply with respect to any tax levied by a county, city, or district pursuant to, or in accordance with, either of those laws.
  - 5) Provides that it is the Legislature's intent to apply the requirements of Revenue and Taxation Code (R&TC) Section 41 to this bill. Specifically, this bill finds and declares the following:
    - a) The goal of this bill's exemption is to help achieve California's greenhouse gas reduction goals and the goal of having 100% of drayage trucks in California be zero-emission by 2035, consistent with Executive Order No. N-79-20, and also incentivize the purchase of new and used zero-emission and near zero-emission drayage trucks as soon as possible;
    - b) The performance indicators related to this bill are as follows:

- i) The annual number of zero-emission and near-zero-emission drayage trucks purchased; and,
  - ii) The annual number of purchased drayage trucks that are not zero-emission or near-zero-emission drayage trucks.
- c) To measure the goals set forth above, the California Department of Tax and Fee Administration (CDTFA) shall measure how many Californians used the SUT exemption and report to the Legislature annually on its findings beginning on and after January 1, 2024. These reports shall be submitted in compliance with Government Code Section 9795.
- 6) Takes effect immediately as a tax levy. However, the provisions of this bill shall become operative on the first day of the first calendar quarter commencing more than 90 days after the effective date of this bill.
- 7) Sunsets this bill's statutory provisions on January 1, 2028.

**EXISTING LAW:**

- 1) Imposes a sales tax on retailers for the privilege of selling tangible personal property (TPP), absent a specific exemption. The tax is based upon the retailer's gross receipts from TPP sales in this state.
- 2) Imposes a complimentary use tax on the storage, use, or other consumption of TPP generally purchased out-of-state and brought into California. The use tax is imposed on the purchaser; and unless the purchaser pays the use tax to an entity registered to collect California's use tax, the purchaser remains liable for the tax. The use tax is set at the same rate as the state's sales tax and must generally be remitted to the CDTFA.
- 3) Requires any bill introduced on or after January 1, 2020, that authorizes a SUT exemption, to contain all of the following:
  - a) Specific goals, purposes, and objectives that the tax expenditure will achieve;
  - b) Detailed performance indicators for the Legislature to use when measuring whether the tax expenditure meets the goals, purposes, and objectives stated in the bill; and,
  - c) Specified data collection requirements to enable the Legislature to determine whether the tax expenditure is meeting, failing to meet, or exceeding those specific goals, purposes, and objectives.

**FISCAL EFFECT:** Staff estimates revenue losses of \$231,000 annually.

**COMMENTS:**

- 1) The author has provided the following statement in support of this bill:

Heavy-duty drayage trucks are a critical part of California's goods movement system, transporting shipments to and from ports and rail facilities. However, commonly used

diesel drayage trucks are a significant source of greenhouse gas emissions and air pollution. Unfortunately, cleaner alternatives are more expensive and subject to numerous taxes and fees. AB 365 will make these cleaner alternatives more affordable by exempting the purchase of new and used zero- and near-zero-emission drayage trucks from the state sales and use tax. This will help to grow the clean technology industry and ensure that individuals and small fleets can afford to do their part to meet the state's ambitious emissions reduction and clean vehicle goals.

2) This bill is supported by the Port of Long Beach, which notes the following:

Despite advancements in clean truck technology, the transition to clean drayage trucks will be an uphill battle due to several issues, including, but not limited to, the price differential between diesel trucks and these newer, cleaner technologies, and the tax due on vehicles that cost approximately \$220,000 for NZE and approximately \$350,000 for ZE. The state tax exemption proposed in AB 365 will help offset the cost of new and used NZE and ZE drayage trucks, making it possible for individuals and small drayage truck fleets to transition to cleaner technology.

As we work to ensure that the nation's maritime commerce continues to move through the unprecedented impacts of the COVID-19 pandemic, the Port of Long Beach remains committed to reducing air quality impacts associated with goods movement. AB 365 will help us accomplish this goal. We respectfully ask that the Assembly Committee on Revenue and Taxation support passage of this bill.

3) This bill is opposed by the California State Association of Counties, which notes:

We appreciate the intent of this measure but unfortunately must oppose it as currently written due to the erosion of revenue for counties. After the past thirty years of changes to sales and use tax allocations, counties now depend on these revenues not only to balance their general fund budgets, but also to directly fund a number of state and federal programs. In fact, the piece of the sales and use tax that funds 2011 Realignment is protected by the California Constitution and the state is required to backfill any reductions. Reducing the sales tax results in direct funding reductions to many realigned and mandated programs, including health care, behavioral health, foster care, and other social services.

California's position as essentially the only state to limit the sales tax only to tangible items has caused a steady erosion of the tax as spending has slowly shifted to services and digital products. Legislation exempting specific products further narrows our already restricted tax base.

4) Committee Staff Comments:

- a) *What is a "tax expenditure"?* Existing law provides various credits, deductions, exclusions, and exemptions for particular taxpayer groups. In the late 1960s, U.S. Treasury officials began arguing that these features of the tax law should be referred to as "expenditures" since they are generally enacted to accomplish some governmental purpose and there is a determinable cost associated with each (in the form of foregone revenues).

As the Department of Finance notes in its annual Tax Expenditure Report, there are several key differences between tax expenditures and direct expenditures. First, tax expenditures are reviewed less frequently than direct expenditures. Second, there is generally no control over the amount of revenue losses associated with any given tax expenditure. Finally, it should also be noted that, once enacted, it takes a two-thirds vote to rescind an existing tax expenditure absent a sunset date. This effectively results in a "one-way ratchet" whereby tax expenditures can be conferred by majority vote, but cannot be rescinded, irrespective of their efficacy or cost, without a supermajority vote.

- b) *An overview of the SUT Law:* The SUT represents the state's second largest source of General Fund (GF) revenues. Nevertheless, the past 70 years have seen a dramatic reduction in the state's reliance on the SUT and a corresponding increase in its reliance on personal income tax revenues. In fiscal year (FY) 2020-21, SUT revenues are estimated to comprise only 18.4% of the state's GF revenues, down from nearly 60% in FY 1950-51.
- c) *What accounts for the state's reduced reliance on SUT revenues?* The SUT Law was enacted in a very different era. In the 1930s, California's economy was largely dominated by manufacturing, and residents mostly bought and sold tangible goods. Thus, in establishing the base for a new consumption tax, it made sense to impose the tax on sales of TPP, defined as personal property that may be "seen, weighed, measured, felt, or touched." Over the past 80 years, however, California's economy has seen dramatic growth in the service and information sectors, resulting in a significant erosion of the SUT base. For example, the Commission on the 21<sup>st</sup> Century Economy noted that spending on taxable goods represented 34.6% of personal income in 2008, down from 55.4% in 1980. As a result, tax experts and economists from across the political spectrum argue that California should expand its SUT base.

It could be argued that, while well-intentioned, additional SUT exemptions further erode an already shrinking SUT base. This, in turn, increases fiscal pressures to maintain or even increase California's relatively high SUT rate. High rates arguably promote non-compliance and encourage out-of-state purchases, placing California retailers at a competitive disadvantage. High rates also risk impacting consumer decision-making, which runs counter to widely accepted principles of sound tax policy.

- d) *What would this bill do?* This bill, on and after January 1, 2023, would exempt from the SUT Law gross receipts from the sale of qualified drayage trucks. CARB notes that today, drayage trucks are generally on-road, diesel-fueled, heavy duty trucks that transport containers and bulk to and from the ports and intermodal railyards as well as to many other locations. In an effort to speed the transition to cleaner alternatives, this bill would confer a partial SUT exemption for trucks that, on or after January 1, 2021, meet the criteria for any of the following clean technology programs:
- i) The California Hybrid and Zero-Emission Truck and Bus Voucher Incentive Project<sup>1</sup>;

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<sup>1</sup> According to its website, this project plays a crucial role in the deployment of zero-emission and near-zero-emission technologies. Specifically, the project responds to a key market challenge by making clean vehicles more affordable for fleets through point-of-purchase price reductions.

- ii) The Carl Moyer Memorial Air Quality Standards Attainment Program<sup>2</sup>; or,
- iii) The Volkswagen Environmental Mitigation Trust for California<sup>3</sup>.

The exemption for such trucks would sunset under this bill on January 1, 2028.

- e) *Executive action:* In recognition of the ongoing climate crisis, Governor Newsom issued Executive Order N-79-20 on September 23, 2020. This order noted that California's long-term economic resilience requires bold action to eliminate emissions from transportation, which is the largest source of emissions in the state. As such, the order provided that, "It shall be a . . . goal of the State that 100 percent of medium- and heavy-duty vehicles in the State be zero-emission by 2045 for all operations where feasible *and by 2035 for drayage trucks.*" (Emphasis added.)
- f) *Policy questions:* Generally, tax expenditures are provided as a matter of legislative grace to encourage taxpayers or consumers to undertake socially beneficial action they may not otherwise undertake absent a financial incentive. There can be no doubt of the social and environmental benefits of speeding the state's transition to a clean transportation infrastructure. That said, the state does not generally provide economic incentives to comply with existing laws, regulations, or executive orders, and doing so may establish a questionable precedent.
- g) *Partial SUT exemptions are complicated to administer:* Most exemptions are applied to the total applicable state and local SUT. However, California does maintain a few partial SUT exemptions: specifically, those for manufacturing and research and development equipment, farm equipment and machinery, diesel fuel used for farming and food processing, teleproduction and postproduction equipment, timber harvesting equipment and machinery, and racehorse breeding stock. These partial exemptions are difficult to process and frequently contain errors. Providing an additional incentive, in the form of a partial SUT exemption, may make the purchase of a qualifying vehicle unnecessarily complicated.
- h) *Suggested technical amendment:* Committee staff suggests adoption of the following technical amendment: Draft language to make the exemption applicable to both gross receipts and sales price to ensure application to use taxes.

## REGISTERED SUPPORT / OPPOSITION:

### Support

Breathe California  
California Association of Port Authorities  
California Electric Transportation Coalition  
California Trucking Association

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<sup>2</sup> The Carl Moyer Memorial Air Quality Standards Attainment Program provides grant funding for cleaner-than-required engines, equipment, and other sources of air pollution. This program is implemented as a partnership between CARB and California's 35 local air districts.

<sup>3</sup> This trust provides about \$423 million for California to mitigate the excess nitrogen oxide (NOx) emissions caused by VW's use of illegal emissions testing defeat devices in certain VW diesel vehicles.

City of Los Angeles  
Port of Los Angeles  
Port of Long Beach  
San Diego Unified Port District  
Valley Industry and Commerce Association

**Opposition**

California State Association of Counties (unless amended)

**Analysis Prepared by:** M. David Ruff / REV. & TAX. / (916) 319-2098