

Date of Hearing: June 20, 2022

ASSEMBLY COMMITTEE ON REVENUE AND TAXATION

Jacqui Irwin, Chair

SB 1266 (Borgeas) – As Amended June 13, 2022

**FOR TESTIMONY ONLY**

Majority vote. Tax levy. Fiscal committee.

**SENATE VOTE:** 38-0

**SUBJECT:** Income taxes: credits: designated wildfire zones

**SUMMARY:** Allows a credit equal to 50% of the amount incurred, subject to specified limitations, by a natural person or a "small business", for the purchase of a "backup electricity generator" or a solar battery for use in a residence or commercial property in a "designated wildfire zone", as defined. Specifically, **this bill:**

- 1) Allows, for taxable years beginning on or after January 1, 2023, and before January 1, 2028, a credit, as specified, for a "qualified expenditure" paid or incurred by a "qualified taxpayer" during the taxable year.
- 2) Allows the credit under both the Personal Income Tax (PIT) Law and the Corporation Tax (CT) Law.
- 3) Provides that the credit amount shall equal 50% of the amount paid or incurred by a "qualified taxpayer" during the taxable year for a "qualified expenditure", subject to the following, as applicable:
  - a) If the "qualified expenditure" is the purchase of a "backup electricity generator", the amount of credit allowed shall not exceed \$3,500 per residence or commercial property, per taxable year; and,
  - b) If the "qualified expenditure" is the purchase of a solar battery, the amount of credit allowed shall not exceed \$5,000 per residence or commercial property, per taxable year.
- 4) Defines a "qualified expenditure" as the purchase of one of the following:
  - a) A "backup electricity generator" for use in a residence or commercial property in a "designated wildfire zone"; or,
  - b) A solar battery for use in a residence or commercial property in a "designated wildfire zone".
- 5) Defines a "qualified taxpayer" as a natural person or a "small business" that incurs a qualified expenditure.

- 6) Defines a "small business" as a business that has average annual gross receipts of \$15 million or less over the previous three taxable years.
- 7) Defines a "backup electricity generator" as a standby or portable device that meets all of the following requirements:
  - a) The device can generate at least 10 kilowatts;
  - b) The device is designed and manufactured exclusively for the purpose of generating electricity; and,
  - c) The device complies with applicable air quality standards promulgated by the California Air Resources Board (CARB).
- 8) Defines a "designated wildfire zone" as territory within a high fire-threat district designated a Tier 3 fire-threat area, as determined by the Public Utilities Commission.
- 9) Provides that, in cases where the credit amount exceeds the taxpayer's tax liability, the excess credit amount may be carried forward to the following taxable year, and succeeding six years if necessary, until the credit is exhausted.
- 10) Provides that the credits' statutory provisions shall only be operative for taxable years for which an appropriation is made in the annual Budget Act or other statute.
- 11) Sunsets the credit statutes on December 1, 2028.
- 12) Provides that, for purposes of complying with Revenue and Taxation Code (R&TC) Section 41, the Legislature finds and declares the following:
  - a) The goal, purpose, or objective of this credit is to encourage the purchase of backup electricity generators or solar batteries that are necessary to protect the health and safety of residents and businesses in designated wildfire zones;
  - b) The performance indicator for the Legislature to use when measuring whether the credit meets this goal is how many taxpayers are allowed the credits; and,
  - c) Notwithstanding R&TC Section 19542, the Franchise Tax Board (FTB) shall annually report to the Legislature on the number of tax returns claiming the credit and the amount of total credits claimed through the 2028 taxable year.
- 13) Takes immediate effect as a tax levy.

**EXISTING LAW:**

- 1) Allows various tax credits under both the PIT Law and the CT Law. These credits are generally designed to encourage socially beneficial behavior or to provide relief to taxpayers that incur specified expenses.
- 2) Allows taxpayers engaged in a trade or business to deduct all expenses that are considered ordinary and necessary in conducting that trade or business.

- 3) Requires any bill authorizing a new credit to contain all of the following:
  - a) Specific goals, purposes, and objectives that the tax credit will achieve;
  - b) Detailed performance indicators for the Legislature to use when measuring whether the tax credit meets the goals, purposes, and objectives stated in the bill; and,
  - c) Data collection requirements to enable the Legislature to determine whether the tax credit is meeting, failing to meet, or exceeding those specific goals, purposes, and objectives. The requirements shall include the specific data and baseline measurements to be collected and remitted in each year the credit is in effect, for the Legislature to measure the change in performance indicators, and the specific taxpayers, state agencies, or other entities required to collect and remit data. (R&TC Section 41.)

**FISCAL EFFECT:** Assuming budgetary authorizations are provided, the FTB has estimated annual General Fund revenue losses of \$44 million in fiscal year (FY) 2022-23, \$90 million in FY 2023-24, and \$100 million in FY 2024-25.

**COMMENTS:**

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

To mitigate the loss of power during Public Safety Power Shut-off events, individuals can utilize sources for back up generation such as generators or batteries. These backup sources of power provide individuals and small businesses the ability to meet specific power needs during de-energization events. Although backup generation and batteries are effective tools to mitigate the loss of power, the issue presented is the cost of these items. Backup generators can cost anywhere from \$2,000 to \$7,000 while back up batteries can range from \$10,000 to \$20,000.

SB 1266 strives to relieve individuals and small businesses in Tier 3 of the Fire Threat Districts of the financial burden associated with purchasing these forms of backup generation. Specifically this bill would create a tax credit not to exceed \$3,500 for the purchase of backup generators and a tax credit not to exceed \$5,000 for batteries for an individual or small business located within Tier 3 of the CPUC Fire Threat Map.

- 2) This bill is supported by Small Business California, which notes the following:

California's wildfire season continues to grow along with the impacts on residents and small businesses. The 2021 wildfire season was the [State's] second worst fire season on record, burning over 2.5 million acres. During severe weather events, utility companies plan power outages to reduce the risk of the systems sparking wildfires.

To mitigate the loss of power during de-energization events, individuals and businesses can utilize sources for back up generation such as generators or batteries. These backup sources of power provide individuals and small businesses the ability to meet specific power needs during these de-energization events.

- 3) This bill is opposed by the California Teachers Association, which notes:

Despite having the 5<sup>th</sup> largest economy in the nation, California continues to rank near the bottom of the states in the nation in per-pupil funding. According to the Education Law Center's *Making the Grade* report, California was ranked 30<sup>th</sup> in per-pupil expenditures, adjusted for regional cost differences for the 2019 fiscal year (the most recent data available). CTA believes that Prop. 98 should be protected from reductions through the creation of new or expanding existing tax expenditures.

4) The FTB notes the following technical considerations in its analysis of this bill:

- a) "This bill would require the FTB to annually report to the legislature on the credits through taxable year 2028. Because tax returns are filed a year in arrears and take time to process, complete data for the first year a tax credit appears on a return is between two years and three years after the taxable year. For instance, the FTB would complete processing of returns for tax year 2023, the first year of the proposed credit, by May 2025. Thus, the earliest that complete data from these returns could be published by the FTB would be approximately May 2025. The author may wish to amend the bill by specifying that data would be published by June beginning in 2025, and annually thereafter, until two years after the sunset date."
- b) "For consistency of terminology within the [R&TC], it is recommended that the phrase 'natural person' within the definition of 'qualified taxpayer' be replaced with 'an individual'."
- c) "For the purposes of the [CT Law], this bill would include in the definition of 'qualified taxpayer' a natural person. Natural persons are subject to taxation under the [PIT Law], not the [CT Law]. It is recommended that 'natural persons' is removed from the definition of 'qualified taxpayer' under the [CT Law] provision."
- d) "Similarly, references to 'residence' should be removed from the [CT Law] provision because taxpayers subject to the [CT Law] do not have a residence."

5) The FTB notes the following policy considerations in its analysis of this bill:

- a) "Because the bill does not specify otherwise:
  - Multiple taxpayers could purchase a generator or solar battery for use at the same residence or commercial property and qualify for the credit.
  - A taxpayer could purchase a generator or solar battery, claim the credit, and not install or use the generator or battery for any length of time or during a power shut off, and qualify for the credit.
  - A taxpayer could purchase a generator or solar battery for use in a residence or commercial property in a designated wildfire zone, claim the credit, and qualify for the credit even if the taxpayer does not own or occupy the residence or commercial property."
- b) "This bill would allow a credit for a backup electricity generator or solar battery that may be currently deductible as a business expense. Generally, a credit is allowed in lieu of a deduction in order to eliminate multiple tax benefits for the same item of expense."

## 6) 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 typically 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) *What would this bill do?* This bill would allow a credit, under both the PIT Law and the CT Law, to encourage the purchase of backup electricity generators and solar batteries in designated wildfire zones. Specifically, the credit would equal 50% of the amount incurred, subject to specified limitations, by a natural person or a small business, as defined, for the purchase of a backup electricity generator or a solar battery for use in a residence or commercial property in a designated wildfire zone.

The author argues that this bill will ensure fewer people are left without power when the state is dealing with a wildfire emergency or public safety power shutoff. The Committee has also been informed that individuals experiencing such power losses have lost groceries, been unable to refrigerate certain medicines, and been forced to relocate to hotels.

- c) *Suboptimal options:* This bill would allow a credit for the purchase of either a solar battery or a backup electricity generator. This bill does not define the term "solar battery", which could lead to administrative confusion and disputes between the FTB and taxpayers seeking the credit. This bill does, however, provide a definition for a "backup electricity generator" and requires such generators to comply with applicable air quality standards promulgated by CARB. According to CARB's website, its regulations specifically allow the use of large diesel generators during a power shut-off event. Moreover, the vast majority of backup electricity generators currently in use (e.g., roughly 90%) are powered by diesel fuel. Diesel generators are a significant source of air pollution, releasing greenhouse gasses, volatile organic compounds, nitrous oxides, and sulfur dioxide. These compounds are known to exacerbate respiratory conditions, such as asthma and chronic obstructive pulmonary disease, especially in children and older adults. Greenhouse gasses also worsen climate change, which leads to more extreme wildfires – wildfires that threaten the very power outages this bill seeks to address.

Advocates, anticipating these concerns, have noted that backup generators allow individuals and businesses a degree of self-sufficiency during planned power shutoffs. These shutoffs, in turn, are undertaken to reduce the risk of wildfires that also release

significant greenhouse gases. To this end, the Copernicus Atmospheric Monitoring Service found that, during a recent three-month period, California fires released more than 75 metric tons of carbon dioxide.

- d) *An incentive or a reward:* As noted above, tax credits are typically conferred to encourage beneficial taxpayer behavior that likely would not occur absent a financial incentive. Reports, however, suggest that backup generator use has already increased significantly. According to a recent report by MCubed using data from the Bay Area Air Quality Management District, the number of nonresidential backup generators in the Bay Area has increased 34% in just three years. If individuals and businesses throughout the state are already purchasing backup generators to contend with future power disruptions, this bill may be providing a reward for actions taxpayers are already taking.
- e) *Committee's tax expenditure policy:* Both R&TC Section 41 and Committee policy require any tax expenditure bill to outline specific goals, purposes, and objectives that the tax expenditure will achieve, along with detailed performance indicators for the Legislature to use when measuring whether the tax expenditure meets those stated goals, purposes, and objectives. A tax expenditure bill will not be eligible for a Committee vote unless it has complied with these requirements.

This bill states that the credit is designed to encourage the purchase of backup electricity generators and solar batteries. In addition, this bill provides that the credit's effectiveness shall be measured by the number of taxpayers allowed the credit. The Committee may wish to consider whether credit utilization, in and of itself, is a sufficient rubric by which to measure this credit's effectiveness.

In addition to the R&TC Section 41 requirements, this Committee's policy also requires that all tax expenditure proposals contain an appropriate sunset provision to be eligible for a vote. According to the policy, an "appropriate sunset provision" means five years, except in the case of a tax expenditure measure providing relief to California veterans, in which case "appropriate sunset provision" means ten years. This bill complies with the Committee's sunset policy.

- f) *Related legislation:* AB 2892 (Bigelow) would have allowed a credit under both the PIT Law and CT Law to encourage the purchase of backup electricity generators in designated wildfire zones. AB 2892 was held in this Committee.

## **REGISTERED SUPPORT / OPPOSITION:**

### **Support**

California Farm Bureau  
Small Business California

### **Opposition**

California Teachers Association

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