

# SUMMARY ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author: Koretz Analyst: Roger Lackey Bill Number: AB 27X

Related Bills: See Prior Analysis Telephone: 845-3627 Amended Date: 03-26-2001

Attorney: Patrick Kusiak Sponsor: \_\_\_\_\_

**SUBJECT:** Power Generation System Credit Or Depreciation Deduction/Sales Tax Credit for Excess Credit

- DEPARTMENT AMENDMENTS ACCEPTED. Amendments reflect suggestions of previous analysis of bill as introduced February 7, 2001.
- AMENDMENTS IMPACT REVENUE. A new revenue estimate is provided.
- AMENDMENTS DID NOT RESOLVE THE DEPARTMENT'S CONCERNS stated in the previous analysis of bill as introduced/amended \_\_\_\_\_.
- FURTHER AMENDMENTS NECESSARY.
- DEPARTMENT POSITION CHANGED TO \_\_\_\_\_.
- REMAINDER OF PREVIOUS ANALYSIS OF BILL AS INTRODUCED February 7, 2001, STILL APPLIES.
- OTHER - See comments below.

## SUMMARY

This bill would:

- Allow a credit for a percentage of the cost to purchase or lease and to install a power generation system.
- Allow a taxpayer to depreciate a power generation system over five years.
- Exempt the purchase of a power generation system from the sales or use tax.
- Allow a retailer to claim a sales or use tax credit equal to the income tax credit described above.

This analysis will address the sales or use tax exemption and the sales or use tax credit for retailers only as they impact the department. This analysis will not address the bill's provisions in the Public Utilities Code or Water Code as they do not impact the department or state income tax revenues.

## SUMMARY OF AMENDMENTS

The March 26, 2001, amendments added the term "Tax Allocation" to the title of the committee and provided that the Tax Allocation Committee would be within the Treasurer's office. The amendments also made a number of technical changes. In addition, the amendments made other changes to the Public Utilities Code.

Board Position:

|                             |                              |   |
|-----------------------------|------------------------------|---|
| <input type="checkbox"/> S  | <input type="checkbox"/> NA  | <input type="checkbox"/> NP                 |
| <input type="checkbox"/> SA | <input type="checkbox"/> O   | <input type="checkbox"/> NAR                |
| <input type="checkbox"/> N  | <input type="checkbox"/> OUA | <input checked="" type="checkbox"/> PENDING |

Legislative Director

Date

Brian Putler

05/17/01

The March 20, 2001, amendments:

- Added language requiring the State Energy Resources and Conservation and Development Commission to certify the power generation systems as necessary for taxpayers to obtain the income tax credit allowed by this bill.
- Created a committee whose purpose would be to allocate the credits, exemptions, and deduction allowed by this bill.
- Capped the amount to be allocated for all benefits at \$50 million.
- Added a sales or use tax credit for retailers. The credit would be equal to the power generation system credit including any carryover amounts.
- Required the taxpayer to make an irrevocable election to claim one of the credits, the exemption, or the deduction.

The March 7, 2001, amendments made the following changes:

- Deleted the sales or use tax credit and added a sales or use tax exemption for power generation systems.
- Revised the power generation system purchase credit and depreciation deduction.
- Revised the claim for refund to the Board of Equalization (BOE) to be a credit for retailers. The credit would be equal to the remaining amount of the power generation system credit at the end of the carryover period. The credit would be applied against sales or use tax for as many years as necessary until it was exhausted. **This provision was deleted by the March 20, 2001, amendments and was replaced by the sales or use tax credit.**

The March 7, 2001, amendments incorporated the language drafted by the department, as requested by the author.

The March 26, March 20, and March 7, 2001, revisions are further discussed under "THIS BILL" below.

As a result of the amendments, a number of the implementation and policy considerations discussed in the department's prior analysis no longer apply. The remaining implementation considerations, including additional implementation considerations, and technical considerations resulting from the later amendments, are included below.

Except for the discussion of this analysis, the department's analysis of AB 27X as amended February 7, 2001, still applies.

## **POSITION**

Pending.

## **THIS BILL**

### **Tax Allocation Committee**

This bill would establish the Tax Allocation Committee (Committee) within the Treasurer's office, consisting of the Director of Finance, the Treasurer, and the Controller. The committee would allocate the respective tax credit or incentive to each qualified taxpayer, in accordance with an unspecified allocation plan.

The aggregate amount of exemptions and credits allowed by this bill could not exceed \$50 million each calendar year.

This bill would give the Committee the authority to promulgate rules, regulations, and procedures to carry out the allocation of the tax credits and incentives added by this bill.

Also, the Committee would report annually to the Legislature regarding the utilization of the tax credits and exemptions allowed by this bill and the activities of the Committee in relation to those incentives.

#### Power Generation Systems Purchase or Lease Credit

This bill would allow a taxpayer to make an irrevocable election to claim a credit for the costs paid or incurred to purchase or lease a power generation system installed and placed in service on property located in California for the production of electricity used onsite.

The power generation system credit would be in lieu of any other credit, exemption, or deduction allowed by this bill, and no deduction would be allowed for any costs for which this credit is claimed.

The applicable percentage of the costs subject to the credit would be:

- 30% for any solar energy, wind-driven, or photovoltaic power generation system,
- 25% for any power generation system placed in service on or after January 1, 2001, and on or before September 1, 2001, and
- 20% for any other power generation system.

“Qualified taxpayer” would mean any taxpayer that purchases or leases a qualified power generation system as an alternative means of supplying its power needs in this state.

“Qualified cost” would mean any cost paid or incurred on or after January 1, 2001, and before January 1, 2006, that satisfies each of the following requirements:

- Is for the purchase or lease of a qualified power generation system that is certified by the Energy Resources Conservation and Development Commission and placed in service in this state,
- Is an amount properly chargeable to the capital account of the taxpayer, and
- Is an amount for which the qualified taxpayer has not elected to claim the enhanced cost recovery deduction or the BOE claim for refund provided by this bill.

“Qualified power generation system” means devices either newly installed or converted from a preexisting power generation system. The system must be used for the individual function of producing electricity at the rate of 50 megawatts or less per day. A “power generation system” includes any solar energy, wind-driven, fuel cell, microturbine, photovoltaic, and natural gas generation system. “Power generation system” does not include any diesel, oil, gasoline, or steam generation system.

This bill also would define “solar energy system,” “wind-driven system,” “fuel cell system,” “microturbine system,” “photovoltaic system,” “natural gas generation system,” “steam generation system,” “compliance period,” “peak load hours,” and “placed in service.”

This bill would provide special rules in the case of a true or operating lease of a power generation system. For these leases, only the taxpayer-lessee that uses the qualified power generation system would be allowed to claim the credit. The inception date of the lease would be considered the “placed in service” date and any non-capital costs (interest factor, maintenance, etc.) would be excluded from the qualified costs used to determine the credit.

This bill would require that 80% of the electricity used by the taxpayer during the taxable year be generated by the power generation system. The bill contains a special rule for calculating the 80% requirement in taxable years that are less than 12 months and for any period during which the qualified power generation system suffers significant operational problems that limit its ability to generate electricity during a taxable year.

If the taxpayer fails to meet the 80% requirement, the taxpayer would be required to recapture a calculated portion of the credit. The recapture would be calculated based on the number of months remaining in the 60-month compliance period.

This bill would require the taxpayer to obtain and retain written certification from the state Energy Resources Conservation and Development Commission that the system is a qualified power generation system.

This bill would allow any excess credit to be carried over and used in the following six taxable years.

#### Power Generation System Depreciation Election

This bill would allow the taxpayer to make an irrevocable election to depreciate the power generation system over five years using the straight-line method of depreciation. This special depreciation deduction would be in lieu of the qualified power generation system credit, or the sales or use tax credit for retailers that file with BOE. The qualified taxpayer would still be required to meet the same requirements of the qualified power generation system credit. If the qualified taxpayer failed to meet those requirements, the qualified taxpayer would be required to recapture the difference between the accelerated special depreciation method and the normal depreciation deduction allowed for a power generation system.

The special depreciation deduction would be in lieu of any other credit or exemption allowed by this bill, or any other deduction allowed for those costs.

#### Sales or Use Tax Credit for Retailers

This bill would allow a taxpayer to make an irrevocable election to claim a sales or use tax credit for retailers required to file a return with the BOE. The credit would be equal to the power generation system credit. The credit would only be allowed if the retailer paid sales tax reimbursement or use tax for the purchase or lease of the power generation system.

The sales or use tax credit would be in lieu of any other credit, exemption, or deduction allowed by this bill.

This bill would require the taxpayer to retain substantiating eligibility for the credit.

The BOE would be required to provide an annual listing to Franchise Tax Board of retailers that claimed the credit.

### IMPLEMENTATION CONCERNS

For the power generation system purchase or lease credit, it is not clear how it would be determined if a power generation system generates at least 80% of the electricity used by the taxpayer, if the power is generated only for onsite usage of the taxpayer, and if that electricity is being used during peak load hours.

The credit is limited to power generation systems used for producing electricity at the rate of 50 megawatts or less per day. It is unclear whether the credit would extend to power generation systems with generating capacity in excess of 50 megawatts per day that actually used for no more than 50 megawatts per day.

The credit for retailers specifies that the credit amount would include any amount that otherwise would exceed the taxpayer's tax liability under the similar income tax credit for the power generation system. However, since the income tax credit would never be taken, no excess amounts would ever exist. Amendment 1 would remove the "excess" reference to the income tax credit.

### TECHNICAL CONSIDERATIONS

Since the bill was amended to no longer allow a claim for refund, Amendments 2, 3, and 4 would eliminate this reference in the other provisions of the bill.

### **ECONOMIC IMPACT**

#### Tax Revenue Estimate

Based on the discussion below, it is projected that all of the annual dollar amount (\$50 million) would be allocated each year.

#### Tax Revenue Discussion

The impact of this bill would depend upon the number of taxpayers and businesses incurring qualifying electric power generation expenses and the average credit applied against tax liabilities.

This bill is expected to have a significant incentive effect, despite the low levels of solar and other alternative type power generators used by taxpayers and businesses in this state. Qualifying electric power generation systems can range significantly. For this analysis the following data and assumptions were used:

- An average cost of approximately \$13,200 for 2001 was used (net of special rebate programs) for a solar energy system installed on single-family homes.
- 1% of all homes will install a solar energy system by 2006.
- An average cost of approximately \$143,000 for 2001 was used (net of special rebate programs) for mid-size systems between 10 kilowatts and 200 kilowatts.

- Average costs were not reduced by allowable federal credits.
- Projected volumes for mid-size systems were based on the California Energy Commission's projected rebate program.
- Assumed in aggregate that 100 megawatts for large systems would be achieved annually after the first full year of implementation.
- Assumed that all other systems would represent approximately 10% of solar systems.
- Assumed in aggregate recapture of credits would not exceed 10% of original claims.
- Adjustments were made to account for offsetting tax effects of deductions for depreciation that would be otherwise allowed under current law.

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FRANCHISE TAX BOARD'S  
PROPOSED AMENDMENTS TO AB 27X  
As Amended March 26, 2001

AMENDMENT 1

On page 6, line 3, after "23684." ~~strikeout the remainder of the line,~~  
and ~~strikeout lines 4 to 6, inclusive,~~ and insert:

If the

AMENDMENT 2

On page 8, line 26, ~~strikeout "filed a claim for refund"~~ and insert:  
claimed a credit

AMENDMENT 3

On page 15, line 34, ~~strikeout "filed a claim for refund"~~ and insert:  
claimed a credit

AMENDMENT 4

On page 22, ~~strikeout lines 18 and 19,~~ and insert:  
Section 23684 or Section 6902.3, any exemption allowed under Section 6367.5, or  
any deduction otherwise allowed by this part for any