Franchise Tax Board

ANALYSIS OF AMENDED BILL

Author:	Anderson	Analyst:	Angela Raygoza	Bill Number:	AB 1853
Related Bills:	See Legislative History	Telephone:	845-7814	Amended Date:	March 6, 2008
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Defensible Space Fire Protection Deduction Within California

SUMMARY

This bill would provide a tax deduction for amounts paid or incurred to create defensible space around specified properties.

SUMMARY OF AMENDMENTS

The March 6, 2008, amendments replaced the intent language of the bill as introduced with language that would provide a tax deduction for amounts paid or incurred to create defensible space.

This is the department's first analysis of this bill.

PURPOSE OF THE BILL

According to the author's office, the purpose of this bill is to encourage taxpayers to protect their homes from wildfires and assist them with complying with the law.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2008, and before January 1, 2012.

POSITION

Pending.

ANALYSIS

FEDERAL/STATE LAW

Existing federal and state laws allow individuals to deduct certain expenses, such as medical expenses, charitable contributions, interest, and taxes, as itemized deductions. Certain other expenses for the production of income and certain employee business expenses are considered miscellaneous itemized deductions and the portion that exceeds 2% of adjusted gross income may be deducted.

Board Position:			Department Director	Date
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Current state and federal laws generally allow taxpayers engaged in a trade or business to deduct all expenses that are considered ordinary and necessary in conducting that trade or business.

Current state law requires landowners in mountainous, forest, brush, and grass-covered lands to maintain a 30-foot firebreak around homes, buildings, and structures. In addition, current state law requires that around and adjacent to an occupied dwelling or occupied structure, *additional* fire protection or firebreaks out to 100 feet from the dwelling or structure or to the property line be maintained. Greater distances may be required by local ordinance, rule, or regulation.

Under the Code of Civil Procedure, a "dwelling" is defined as a place where a person resides and may include, but is not limited to, the following:

- A house together with the outbuildings and the land upon which they are situated.
- A mobile home together with the outbuildings and the land upon which they are situated.
- A boat or other waterborne vessel.
- A condominium, as defined in Section 783 of the Civil Code.

<u>THIS BILL</u>

For each taxable year beginning on or after January 1, 2008, and before January 1, 2012, this bill would provide a tax deduction in an amount equal to the qualified costs paid or incurred by a taxpayer to create a defensible space under the Personal Income Tax Law (PITL) and the Corporation Tax Law (CTL). The maximum deduction allowed is $500 dollars for each qualified property.

This bill would define the following terms:

- "Defensible Space" means the area created by removing all brush, flammable vegetation, and combustible growth that is located within 100 feet of the structural components of a dwelling located on a qualified property.
- "Dwelling" has the same meaning as described in section 704.710 of the Code of Civil Procedure but excludes a boat or other waterborne vessel.
- "Fire Department" means the local fire department that has jurisdiction over the qualified property.
- "Licensed Contractor" means a contractor with an active license issued by the Contractors' State License Board.
- "Qualified costs" means 25 percent of the costs paid or incurred by a qualified taxpayer for labor and services performed by a licensed contractor to create a defensible space around a qualified property, which costs are evidenced by records and documents including, but not limited to, a written certification.
- "Qualified property" means any dwelling located within California.
- "Qualified taxpayer" means any taxpayer that owns qualified property.
- "Written Certification" means a written evaluation by the fire department that certifies the establishment of defensible space, provided that the certification shall be obtained within 30 days after completion of the work establishing the defensible space. The taxpayer shall retain a copy of the certification and provide it to the Franchise Tax Board (FTB) upon request.

In order to receive a deduction, this bill requires that a qualified taxpayer provide written certification, upon request, to the FTB.

This bill specifies that any deduction allowed under the personal income tax or corporate tax laws should not be reduced by the amount of the deduction for qualified costs allowed under this bill.

This deduction would be repealed as of December 1, 2012.

IMPLEMENTATION CONSIDERATIONS

Implementing this bill would occur during the department's normal annual update.

OTHER STATES INFORMATION

The states surveyed include *Florida, Illinois, Massachusetts, Michigan, Minnesota,* and *New York.* These states were selected due to their similarities to California's economy, business entity types, and tax laws. These states do not have a deduction comparable to the deduction provided in this bill.

FISCAL IMPACT

This bill would not significantly impact the department's costs.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue losses:

Estimated Revenue Impact of AB1853 Effective for Tax Years BOA January 1, 2008 ($ in Millions)		
2008-09	2009-10	2010-11
-$1	-$6	-$5

Enactment is assumed after June 30, 2008. This analysis does not account for changes in employment, personal income, or gross state product that could result from this bill.

Revenue Discussion

The revenue impact of this bill would depend on the number of qualified taxpayers who hire a licensed contractor to create a defensible space, qualified costs, and required certification by the appropriate fire department within 30 days after completion of the work.

The Department of Finance reports 13,312,456 qualified properties are located in California. Based on taxpayer behavior it is assumed 5% or 665,623 owners (13,312,456 x 5% = 665,623) of qualified properties would participate during the 4 years this deduction would be allowed and pay $1,500 as the average cost for a licensed contractor to clear up to 100 feet of defensible space.

As a result, there would be approximately $250 million in potential deductions ($1500 x 25% limitation = $375; $375 x 665,623 ≈ $250 million).

Based on average taxpayer liability, it is estimated that 20% of the $250 million, or $50 million, in total deductions would be deducted by business entities. Applying a corporate tax rate of 8% (to account for S-corporation's tax rate and minimum tax corporations) would result in a $4 million business entity tax revenue loss ($50 million x 8% = $4 million). For individuals, a 6% marginal tax rate would be applied to the remaining deduction of $200 million, which would result in a $12 million individual tax revenue loss ($200 million x 6% = $12 million).

The total revenue loss from business entities and individuals is projected to be $16 million ($12 million + $4 million = $16 million) over 4 years. Due to the start up of the required certification process, it is assumed that $800,000 or 5% would be claimed in tax year 2008, 35% or approximately $6 million in tax years 2009 and 2010, and 25% or $4 million in tax year 2011. The estimate in the chart reflects the fiscal year effects of reduced estimated tax payments and returns filed claiming the deduction.

POLICY CONCERN

This bill would allow taxpayers in certain circumstances to claim multiple tax benefits for the same item of expense. In addition, it would provide an incentive to create a defensible space that is required by existing state and federal laws or regulations.

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