

ANALYSIS OF ORIGINAL BILL

Franchise Tax Board

Author: Florez Analyst: John Pavalasky Bill Number: SB 73

Related Bills: See Legislative History Telephone: 845-5163 Introduced Date: January 17, 2007

Attorney: Daniel Biedler Sponsor: _____

SUBJECT: Biodiesel Fuel Refundable Credit

SUMMARY

This bill would allow a refundable tax credit for each gallon of biodiesel fuel that is produced or manufactured at any facility located in California.

PURPOSE OF THE BILL

According to the author's office, the purpose of this bill is to promote participation by producers in California's biodiesel industry, working toward satisfying the Governor's goal of domestic production for a minimum of 20% of the fuel consumed in California.

EFFECTIVE/OPERATIVE DATE

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

POSITION

Pending.

SUMMARY OF SUGGESTED AMENDMENTS

Technical amendments are necessary and are provided in the discussion of TECHNICAL CONSIDERATIONS. Department personnel are available to work with the author to resolve the implementation issues discussed in this analysis, as well as any other issues that arise as the bill moves through the legislative process.

ANALYSIS

FEDERAL/STATE LAW

Federal law currently allows a biodiesel and renewable diesel fuels credit. The credit is equal to \$.50 for each gallon of biodiesel that is used by a taxpayer as fuel in a trade or business or sold at retail and placed in the fuel tank of the buyer's vehicle.

Board Position:

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Department Director

Date

Selvi Stanislaus

3/9/07

Existing state laws provide various credits for personal income tax that reduce the tax and have either refundable or carryover provisions. Corporate tax laws provide various credits that reduce the tax and in some instances have carryover provisions. Generally, these credits are designed to provide incentives for taxpayers to perform various actions or activities that they may not otherwise undertake.

THIS BILL

This bill would allow, for each taxable year beginning on or after January 1, 2008, a credit of \$.30 for each gallon of biodiesel fuel produced or manufactured during the taxable year by a qualified producer at any facility located in California.

The credit allowed cannot exceed a cumulative amount of thirty million gallons per taxable year, as produced or manufactured by all qualified producers who receive this credit.

“Biodiesel fuel” is defined as a renewable, biodegradable, mono alkyl ester combustible liquid fuel derived from vegetable oils or animal fats that meet the American Society for Testing and Materials specification for biodiesel fuel (B100) blend stock for distillate fuels. Therefore, the biodiesel fuel produced or manufactured that is eligible for credit must be of 100% biodiesel and not some lesser amount of biodiesel blended with diesel fuel.

“Facility” is defined as a qualified producer’s refinery located in California that produces or manufactures biodiesel fuel.

“Qualified producer” is defined as any person that owns or operates a facility and that is engaged in the production or manufacture of biodiesel fuel at that facility.

This bill would require that within 25 days after the end of each calendar quarter, each qualified producer would be required to substantiate the total amount of biodiesel fuel that was produced or manufactured during the previous calendar quarter. This information would be submitted to the Franchise Tax Board (FTB) as required.

This bill specifies that if the credit allowed exceeds the taxpayer's liability, the excess would be credited against other amounts due. Any remaining credit would be refunded on a quarterly basis to the qualified producer by the Treasurer.

FTB would be required to submit a quarterly list to the Treasurer of the qualified producers that are eligible to receive a refund; Treasurer would be required to make the refunds from the State Highway Account.

IMPLEMENTATION CONSIDERATIONS

The department has identified the following implementation concerns. Department staff is available to work with the author’s office to resolve these and other concerns that may be identified.

- This bill would allow the credit on an annual taxable year basis and require the department to submit a quarterly list to the Treasurer of the qualified producers that are eligible to receive a refund. Thus, the Treasurer rather than the department would be making

refunds from the State Highway Account. For calendar year taxpayers the 2008 returns for corporations are due beginning on March 15, 2009, while 2008 returns are due from noncorporate taxpayers beginning April 15, 2009. Returns for fiscal year taxpayers are filed beginning 2 ½ months after the end of their fiscal year. Additionally, six month extensions of these filing due dates are automatically allowed. Therefore the first list from the department to the Treasurer of the qualified producers who are eligible to receive a refund under the bill would be required to be made on March 31, 2009, leaving the department little time to process the returns and validate eligibility for a refund through an audit. The author may wish to provide specifically that the quarterly list requirement from the department for taxable year 2008 and subsequent taxable years does not commence until all of the tax returns for that taxable year have been required to be filed.

- This bill lacks direction for certification and reporting requirements to substantiate the total amount of biodiesel fuel produced by a qualified producer for the taxable year that qualifies for the credit under the standard proposed by the bill (D100). It is also unknown who will be responsible for tracking the total limit on eligible biodiesel fuel that is produced in each taxable year. If the department would be responsible for this, it would require a tracking system and would result in a significant impact on the department's operations and costs. Often credits requiring this type of specialized expertise are enacted or proposed using the appropriate state agency that possesses this expertise for allocation and certification purposes, and then the department can receive the necessary information from the appropriate state agency.
- This bill uses terms that are undefined, including "refinery," "person," "owns or operates," and "who is engaged in the production or manufacture of biodiesel fuel." The absence of definitions to clarify terms could lead to disputes with taxpayers and would complicate the administration of this credit.
- The authority to make regulations contained in the bill does not provide the specific grant of legislative authority that is needed for those regulations to be considered "legislative regulations" in a manner similar to the "legislative regulations" authorized in Revenue and Taxation Code section 18152.5(k) relating to small business stock. Without a grant of "legislative regulation" authority, the statutory provisions themselves would need to detail all the rules necessary to implement these credits.
- This bill fails to modify the hierarchy of Corporation Tax Law (CTL) credits. It is unclear in what order this credit would be applied in determining the "tax" under the CTL for the taxable year. The existing hierarchy under personal income tax law (PITL) includes credits that contain refundable provisions.
- This bill leaves unclear whether partners or shareholders in pass-through entities (partnerships, including limited liability companies classified as partnerships and S corporations) that are "qualified producers" could themselves be considered "qualified producers" and be eligible to claim the credit and receive the refund, or whether the department would be required to list only the pass-through entity that is a "qualified producer" as eligible to receive a refund from the Treasurer. The lack of guidance could cause disputes between taxpayers and the department.

TECHNICAL CONSIDERATIONS

A cross reference in the bill is incorrect. On page 3, line 14, strikeout "Section 1705363" and insert Section 17053.63.

OTHER STATES' INFORMATION

The laws of the following states were reviewed because their tax laws are similar to California's income tax laws, and provide a credit comparable to the credit allowed by this bill.

Florida allows for tax years beginning on or after January 1, 2007, a credit against either the corporate income tax or the franchise tax in an amount equal to the eligible costs in connection with an investment in the production, storage, and distribution of biodiesel in the state, including the costs of constructing, installing, and equipping such technologies in the state. Credits that exceed the corporation's tax liability can be carried forward until the expiration date of December 31, 2012.

New York allows a credit equal to \$.01 for each percent of biodiesel per gallon of bioheat purchased on or after July 1, 2006, and before July 1, 2007, for tax years beginning in 2006 and 2007. The maximum credit is \$.20 per gallon. The credit reduces the tax liability and includes carryover provisions.

Florida, Illinois, and Minnesota allow an exemption from sales and use tax on the sale of biodiesel fuel that is 10% biodiesel or more.

FISCAL IMPACT

The department's costs to administer this bill cannot be determined until implementation concerns have been resolved but are anticipated to be significant.

This bill would require a quarterly listing to be made by the department to the Treasurer of the qualified producers that are eligible to receive a refund. As a result, this bill would impact the department's audit costs as well as printing, processing, and storage costs for tax returns. The additional costs have not been determined at this time. If the bill continues to move through the legislative process, costs will be identified and an appropriation will be requested.

ECONOMIC IMPACT

Revenue Estimate

Based on data and assumptions discussed below, this bill would result in the following revenue losses.

Estimated Revenue Impact of SB 73 Effective for Tax Years BOA 1/1/2008 Assumed Enactment After 6/30/07 (\$ in Millions)		
07/08	08/09	09/10
< -\$0.5	-\$5	-\$8

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this bill.

Revenue Discussion

The California Energy Commission projects biodiesel fuel production in California to total 39 million gallons in 2008. This bill, however, would provide an aggregate limit on creditable qualified biodiesel fuel produced or manufactured in any taxable year to 30 million gallons, totaling a maximum of \$9 million in credits (30 mil. gallons x 30 cents = \$9 million) in any taxable year. A portion of these credits would reduce income tax liabilities and unused credits would be refunded. Based on a review of tax returns of potentially qualified taxpayers, this estimate uses a refundable rate of 95% or \$8.5 million (\$9 million x 95%).

Based on a review of taxable year periods for biodiesel fuel companies, calendar year versus fiscal year filers are split 50/50. This taxable year split amongst taxpayers means that credits generated by taxpayers during a taxable year will impact cash flow fiscal year estimates in multiple fiscal years. Therefore, of the \$8.5 million credits available for refund for taxable year 2008, only 3% would impact fiscal year 07/08, resulting in a minor revenue loss of less than \$500,000 (\$8.5 million x 3% = \$255,000) shown in the table. This is due to anticipated changes to estimated payments throughout 2008.

ARGUMENTS/POLICY CONCERNS

The California Energy Commission projects biodiesel fuel production in California to total 39 million gallons in 2008. This bill, however, would limit qualified biodiesel fuel available for credit in any year to 30 million gallons. Therefore, this bill may not provide an incentive effect but instead simply reward those qualified producers that already are producing biodiesel fuel.

LEGISLATIVE STAFF CONTACT

John Pavalasky
Franchise Tax Board
845-5163
john.pavalasky@ftb.ca.gov

Brian Putler
Franchise Tax Board
845-6333
brian.putler@ftb.ca.gov