BILL ANALYSIS

Department, Board, Or Commission	Author	Bill Number
Franchise Tax Board	**Hill**	**AB 50**

SUBJECT

Exclusion/Compensation Received From PG&E/San Bruno Gas Explosion

SUMMARY

This bill would do the following for the victims of the September 9, 2010, San Bruno natural gas transmission line explosion and fire (hereinafter "explosion"):

- Make disaster relief payments received not taxable for state purposes within the meaning of current disaster relief laws, and
- Make gains from the involuntary conversion of destroyed property not taxable for state purposes within the meaning of current federal involuntary conversion laws.

PURPOSE OF BILL

According to the author's office, the purpose of the bill is to prevent victims of the explosion from suffering further harm by incurring a tax obligation on compensation received from PG&E.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately upon enactment and specifically operative for payments made to victims of the explosion or after September 9, 2010. The provision regarding involuntary conversions would be operative for taxable years beginning on or after January 1, 2011.

ANALYSIS

<u>FEDERAL/STATE LAW</u>

Existing federal and state laws provide that gross income includes all income from whatever source derived, including compensation for services, business income, gains from property, interest, dividends, rents, and royalties, unless specifically excluded.

Current federal and state laws allow taxpayers to exclude the following from gross income:

- Amounts received as a result of a fire, flood, or other casualty if the amounts are received by an individual under an insurance contract;
- Gain from the sale or exchange of property if the property, for two of the five years prior to the sale, was owned and used as the taxpayer's principal residence. The allowable exclusion is $250,000 ($500,000 for taxpayers who are married filing jointly);

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- Gain from the involuntary conversion of property, resulting from destruction, into similar property[1] or into money used to acquire replacement property within a specified period. "Involuntary conversion" means the replacement of property that was destroyed through no fault of the owner; and
- Disaster relief compensation made for qualified disasters, with limitations as described below.

Current federal[2] and state tax laws allow disaster relief compensation made to individuals because of a qualified disaster to be excluded from gross income only to the extent that the funds are used for either of the following:

- To pay for personal, family, living, or funeral expenses that were incurred as a result of the qualifying disaster.
- To pay for expenses for rehabilitation or replacement of a personal residence or rehabilitation or replacement of belongings incurred as a result of the qualifying disaster.

Disaster relief compensation is excludable only to the extent that any expense is not already compensated by insurance or otherwise.

A qualified disaster is defined as a disaster which results from a terroristic or military action (as defined in IRC section 692(c)(2)), a Presidentially declared disaster, a disaster which results from an accident involving a common carrier or from any other event which would be determined by the Secretary to be of a catastrophic nature, or, for purposes of payments made by a Federal, State or local government, a disaster designated by Federal, State or local authorities to warrant assistance.

<u>THIS BILL</u>

This bill would deem the San Bruno explosion to be a qualified federal disaster for state purposes, thus treating payments to individuals who were victims of the explosion as qualified disaster relief payments. As a result, payments made to the victims of the explosion used for reasonable and necessary living expenses, to the extent victims were not already reimbursed by insurance or otherwise, would be excluded from gross income (not taxed by California). (Because the explosion was not declared a federal disaster at the time of this analysis, payments received by victims of the explosion would be taxable for federal purposes.)

Further, this bill, under the Personal Income Tax Law, would deem involuntary conversions of property that occurred as a result of the explosion to be a federally declared disaster for state purposes. Taxpayers who have a gain from an involuntary conversion may elect to defer paying tax on that gain by purchasing similar replacement property within a specific period, generally two years after the close of the first taxable year in which any part of the gain is realized.

[1] Any gain is deferred until the sale of the replacement property.
[2] Internal Revenue Code section 139.

LEGISLATIVE HISTORY

ABX6 11 (Hill, Stats. 2010, 6th Ex. Sess. Ch. 2) allows disaster loss treatment for losses sustained as a result of the explosion and fire that occurred in San Mateo County in September 2010.

OTHER STATES' INFORMATION

Illinois, Massachusetts, Minnesota, and *New York* conform to the federal provisions related to gross income exclusions for disaster losses and involuntary conversions. As a result, compensation received due to a specified disaster or income received from an involuntary conversion of property is automatically excluded from income in these states. Similarly, it appears that legislation, executive order, or proclamation by the President or the Governor is required to identify the area impacted by a disaster that is eligible for federal or state assistance.

Florida has no personal income tax, thus its laws are not applicable.

These states were reviewed because of the similarities between California income tax laws and their tax laws.

FISCAL IMPACT

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

ECONOMIC IMPACT

Estimated Revenue Impact of AB 50		
PG&E Immediate Relief Payments For payments made On or After September 9, 2010 Enactment Assumed After June 30, 2011		
2010-11	2011-12	2012-13
$ -300,000	$ -6,000	$ 0

This estimate does not account for changes in employment, personal income, or gross state product that could result from this bill.

This estimate assumes the disaster relief payments received from PG&E for damages is one hundred percent taxable at the federal level because the explosion has not been declared a disaster for federal purposes. There is no revenue associated with involuntary conversions made as a result of the explosion. The revenue impact takes into consideration that this bill limits the taxability of payments received to only those amounts that would have been taxable under federal law had the San Bruno explosion been declared a disaster under federal law. This estimate may be revised in the event the Treasury Department makes a determination that some compensation from PG&E is not includable in gross income.

Appointments

None.

Support/Opposition

Support: Pacific Gas and Electric Company; American Federation of State, County and Municipal Employees (AFSCME); AFL-CIO

Opposition: None provided.

VOTES

Concurrence	03/29/11	Y: 75	N: 0
Assembly Floor	03/03/11	Y: 75	N: 0
Senate Floor	03/24/11	Y: 37	N: 0

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