ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author:	Grove	Analyst:	Jessica Deitchman	Bill Number:	AB 2537
Related Bills:	See Legislative History	Telephone:	845-6310	Amended Date:	April 1, 2014
		Attorney:	Bruce Langston	Sponsor:	

SUBJECT: Water Conserving Plumbing Fixtures Credit

SUMMARY

This bill would, under the Personal Income Tax Law (PITL) and Corporation Tax Law (CTL), allow a credit for the installation of water-conserving plumbing fixtures.

RECOMMENDATION

No position.

Summary of Amendments

The April 1, 2014, amendments removed the language that would have made a technical, non-substantive change to the definition of non-resident in the bill, and replaced it with the provisions discussed in this analysis. This is the department's first analysis of the bill.

REASON FOR THE BILL

The reason for the bill is to address the state's need to conserve water by providing a tax credit to provide an additional tax incentive to encourage taxpayers to upgrade plumbing fixtures on their properties to ones that conserve water.

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, 2014.

ANALYSIS

FEDERAL/STATE LAW

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.

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Existing state and federal laws provide various tax credits designed to provide tax relief for taxpayers who incur certain expenses (e.g., child adoption) or to influence behavior, including business practices and decisions (e.g., research credits or economic development area hiring credits). These credits generally are designed to provide incentives for taxpayers to perform various actions or activities that they may not otherwise undertake.

Current California law[1] requires, by January 1, 2019, that all noncompliant plumbing fixtures in multifamily residential real property and commercial real property be replaced with water-conserving plumbing fixtures.

Current state law lacks a comparable credit to the one that would be created by this bill.

Federal law provides a credit for energy efficient upgrades such as solar or wind energy, but lacks a credit for installing water-conserving plumbing fixtures.

<u>THIS BILL</u>

For taxable years beginning on or after January 1, 2014, this bill would, under both the PITL and CTL, provide a qualified taxpayer a tax credit of 25 percent of the qualified costs paid or incurred for the installation of one or more water-conserving plumbing fixtures by a licensed plumber to replace a noncompliant plumbing fixture on qualified real property in this state, not to exceed $2,500 per taxable year per qualified taxpayer.

The bill would define the following phrases:

- “Qualified taxpayer” means the owner of any qualified real property.
- “Water-conserving plumbing fixture” means any fixture that is in compliance with current building standards applicable to a newly constructed real properly of the same type.
- “ Noncompliant plumbing fixture means any of the following:
    - Any toilet manufactured to use more than 1.6 gallons of water per flush.
    - Any urinal manufactured to use more than one gallon of water per flush.
    - Any showerhead manufactured to have a flow capacity of more than 2.5 gallons of water per minute.
    - Any interior faucet that emits more than 2.2 gallons of water per minute.
- “Qualified real property” means any of the following:
    - Commercial real property –means any real property that is improved with, or consisting of, a building that is intended for commercial use, including hotels and motels, that is not a single-family residential real property or a multifamily residential real property.
    - Multifamily residential real property – means any real property that is improved with, or consisting of, a building containing more than one unit that is intended for human habitation, or any mixed residential-commercial buildings or portions thereof that are intended for human habitation. Multifamily residential includes residential hotels but does not include hotels and motels that are not residential hotels.

[1] Civil law Code Section 1101.4 and 1101.5

- Single-family residential real property – means any real property that is improved with, or consisting of, a building containing not more than one unit that is intended for human habitation.

Qualified real property excludes any real property for which water service is permanently disconnected.

This bill would require that the qualified taxpayer obtain a certification from a licensed plumber that the plumber installed a water-conserving plumbing fixture to replace a noncompliant plumbing fixture on qualified real property in this state.

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.

The bill requires that taxpayers use a licensed plumber to install the water-conserving item. This would preclude taxpayers that install the item themselves from getting the credit for the cost of the water-conserving item installed. If this is contrary to the author's intent, the bill should be amended.

Because the bill fails to specify otherwise, the $2,500 annual cap on the credit would apply to each owner of a qualified property. For example, a qualified property owned by two qualified taxpayers could generate a credit of up to $5,000. If this is contrary to the author's intent, the bill should be amended to specify that the $2,500 per year is per property.

LEGISLATIVE HISTORY

AB 1510 (Pan, 2013/2014), would allow a tax credit equal to 30 percent of a taxpayer's qualified costs to retrofit a qualified building that is an at-risk property. AB 1510 was introduced on April 1, 2014.

OTHER STATES' INFORMATION

Florida, Illinois, Massachusetts, Michigan, Minnesota, and *New York* laws do not provide a credit comparable to the credit allowed by this bill. The laws of these states were selected due to their similarities to California's economy, business entity types, and tax laws.

FISCAL IMPACT

Costs have not been determined at this time. As the bill continues to move through the legislative process and the implementation concerns are resolved, costs will be identified and an appropriation will be requested, if necessary.

ECONOMIC IMPACT

Revenue Estimate

Estimated Revenue Impact of AB 2537 As Amended April 1, 2014 Assumed Enactment After June 30, 2014 ($ in Millions)		
2014-15	2015-16	2016-17
- $300	- $230	- $90

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

SUPPORT/OPPOSITION

Support: None provided.

Opposition: None provided.

ARGUMENTS

Proponents: Some may argue that the bill would assist in easing California's drought by encouraging taxpayers to upgrade plumbing fixtures to conserve water.

Opponents: Some may argue that water conservation is a critical state interest and should be more robustly encouraged by expanding the credit to all installations of state-of-the-are water conserving fixtures and appliances.

POLICY CONCERNS

Generally tax credits are enacted to provide incentives for taxpayers to perform various actions or activities that they may not otherwise undertake. Because current law requires that properties be upgraded with water efficient plumbing, this bill would be providing a tax credit for an action that is mandated by law.

This bill would allow a credit for replacement of plumbing with water-efficient items. These repairs or upgrades are currently deductible as business expenses. Generally, a credit is allowed in lieu of a deduction in order to eliminate multiple tax benefits for the same item of expense.

This bill lacks carryover language. As a result, any unused credit would be lost if the taxpayer is unable to use the entire credit amount in the year claimed. The author may wish to add language allowing a limited carryover period.

This bill lacks a sunset date. Sunset dates generally are provided to allow periodic review of the effectiveness of the credit by the Legislature.

LEGISLATIVE STAFF CONTACT

Jessica Deitchman	Mandy Hayes	Jahna Carlson
Legislative Analyst, FTB	Revenue Manager, FTB	Asst. Legislative Director, FTB
(916) 845-6310	(916) 845-5125	(916) 845-5683
jessica.deitchman@ftb.ca.gov	mandy.hayes@ftb.ca.gov	jahna.carlson@ftb.ca.gov