

# ANALYSIS OF ORIGINAL BILL

Author: Patterson & Chavez Analyst: Jessica Deitchman Bill Number: AB 1329  
 Related Bills: See Legislative History Telephone: 845-6310 Introduced Date: February 27, 2015  
 Attorney: Bruce Langston Sponsor \_\_\_\_\_

<b>SUBJECT:</b>	Defensible Space for Fuel Management Activities Credit
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## SUMMARY

This bill would, under the Personal Income Tax Law (PITL), allow a tax credit for costs paid to create defensible space on real property.

## RECOMMENDATION

No position.

## Summary of Suggested Amendments

An amendment is provided to make a technical correction.

## REASON FOR THE BILL

The reason for the bill is to encourage all Californians to create a defensible space to prevent wildfires.

## 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, 2016.

## 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.

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 federal and state laws lack a credit comparable to the one that would be created by this bill.

Board Position:	Executive Officer	Date
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Current state law<sup>1</sup> requires homeowners to keep a “defensible space” clearance around homes and structures of at least 100 feet.

## **THIS BILL**

For taxable years beginning on or after January 1, 2016, this bill would allow a credit equal to 25 percent of the amounts paid or incurred by a qualified taxpayer during the taxable year for fuel management activities performed on qualified real property.

The amount of credit allowed by this bill could not exceed the lesser of:

- \$2,500 per qualified taxpayer per taxable year, or
- 50 percent of a qualified taxpayer’s total tax for that year.

A deduction would not be allowed for any amount paid or incurred for which a credit is allowed.

This bill would require the Franchise Tax Board (FTB) to establish a procedure to verify that the amount was paid or incurred by the qualified taxpayer for fuel management activities on qualified property.

The bill would define the following:

- “Defensible space” would mean the area adjacent to a structure or dwelling where wildfire prevention or protection practices are implemented to provide defense from an approaching wildfire or to minimize the spread of a structure fire to wildlands or surrounding areas.
- “Fuel management activities” would mean any of the following, provided that the activity meets or exceeds the requirements of the 2015 California Forest Practice Rules:
  - the creation of a defensible space around structures,
  - the establishment of fuel breaks,
  - the thinning of woody vegetation for the primary purpose of reducing risk to structures from wildfire,
  - the secondary treatment of woody fuel by looping, scattering, piling, chipping, or removing from the site, or
  - prescribed burning.<sup>2</sup>
- “Hazardous fire area” would have the same meaning as defined in Section 4251 of the Public Resources Code.<sup>3</sup>

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<sup>1</sup> Government Code section 51182.

<sup>2</sup> Provided these activities meet or exceed the requirements of the 2015 California Forest Practice Rules.

<sup>3</sup> Means any area which is designated as a hazardous fire area by the board or director.

- “Qualified real property” would mean real property that is located within a hazardous fire area or a very high fire hazard severity zone in this state.
- “Qualified taxpayer” would mean a taxpayer who owns qualified real property. A taxpayer who owns a share of qualified real property may be allowed a share of the credit based on the taxpayer’s share of the qualified costs.
- “Wildfire” would mean an unplanned, unwanted wildland fire, including unauthorized human-caused fires, escaped wildland fire use events, escaped prescribed fire projects and all other wildland fires where the objective is to extinguish the fire.
- “Very high fire hazard severity zone” would have the same meaning as that term is defined in subdivision (i) of Section 51177 of the Government Code.<sup>4</sup>

This bill would specify that it is the intent of the legislature to enact legislation to comply with the requirements of Revenue and Taxation Code (R&TC) section 41.<sup>5</sup>

### **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 uses a term that is undefined, i.e., “total tax.” The absence of a definition to clarify this term could lead to disputes with taxpayers and would complicate the administration of this credit. To remain consistent in terminology used in the tax code, it is recommended the bill be amended to use the term “tax liability” instead of “total tax.”

The bill would allow a credit for costs paid or incurred for fuel management activities to create a “defensible space,” as defined. This bill may be overly broad and it is unclear what costs would and should be included in the calculation for the credit. The absence of clarity for this term could lead to disputes between taxpayers and the department and would complicate the administration of this credit.

This bill would require the FTB to establish a procedure to verify that a taxpayer meets the criteria in order to receive the credit. Typically, credits involving areas for which the department lacks expertise are certified by another agency or agencies that possess the relevant expertise. The certification language would specify the responsibilities of both the certifying agency and the taxpayer. It is recommended that this bill be amended to include a certifying agency.

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<sup>4</sup> Means an area designated by the director pursuant to Section 51178 that is not a state responsibility area.

<sup>5</sup> R&TC section 41 requires any new tax credit legislation introduced on or after January 1, 2015, to include specific goals, purposes, objectives, and performance measures.

Because the bill fails to specify otherwise, the FTB would be subject to the rulemaking procedures required under the Administrative Procedures Act (APA).<sup>6</sup> Following these procedures may delay the immediate implementation of this bill. To prevent any delay, it is recommended that the author add a provision exempting the FTB from the APA when the FTB is prescribing rules, guidelines, or procedures necessary or appropriate to carry out the purpose of this bill.

The bill would allow a credit equal to no more than 50 percent of the qualified taxpayer's total tax for the taxable year. It is unclear how the FTB or the taxpayer would know the total tax until the relevant return is filed and accepted. Further, it is unclear how much credit should be allowed for properties owned by multiple qualified taxpayers. The bill states that the credit could not exceed 50 percent of the tax for the taxpayer; is that 50 percent of each taxpayer's tax liability combined or separate? If the intent is combined, it is unclear how the department would know how much credit should be allowed when a single owner's return is received. Because it would be problematic to allow a credit on an amount that is unknown until the return is filed and accepted, it is recommended the bill be amended to specifically address that the credit is capped at 50 percent of each individual owner's tax liability from a previous taxable year or to use another method of capping the credit.

Further, it is unclear how other credits might be applied to determine the amount of the taxpayer's "total tax" to calculate the 50 percent cap. It is recommended the bill be amended to specify the order that other credits should be applied.

Because the bill specifies that prescribed burning would be allowed "provided these activities meet or exceed the requirements of the 2015 California Forest Practice Rules," the rules as they exist for 2015 would be the only rules considered in future years. If this is contrary to the author's intent, the bill should be amended.

## **TECHNICAL CONSIDERATIONS**

There are two periods on page 2, line 32 after "fire." For grammatical accuracy, one of the periods should be deleted.

## **LEGISLATIVE HISTORY**

AB 294 (Anderson, 2009/2010) would have provided a tax deduction in an amount equal to the cost paid or incurred by a taxpayer to create a defensible space, not to exceed \$500 for each qualified property. AB 294 failed passage out of the Assembly Revenue and Taxation Committee.

AB 363 (Miller 2009/2010) would have created a tax credit for the costs incurred to bring a qualified home into fire safety compliance, as specified. AB 363 failed passage out of the Assembly Revenue and Taxation Committee.

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<sup>6</sup> Government Code section 11340.

AB 424 (Gaines, 2007/2008) would have allowed taxpayers a credit equal to, but not greater than \$500, for qualified costs incurred for creating a defensible space around an existing home. AB 424 failed passage out of the Senate Revenue and Taxation Committee.

AB 1853 (Anderson, 2007/2008) would have provided a tax deduction for amounts paid or incurred to create defensible space around specified properties. AB 1853 failed passage out of the Assembly Revenue and Taxation Committee.

AB 1912 (Plescia, 2007/2008) would have provided a credit in an amount equal to 15 percent of the costs paid or incurred by a taxpayer for the purchase and installation of any wildfire risk reduction improvement installed on existing property in this state. AB 1912 failed passage out of the Assembly Revenue and Taxation Committee.

### 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. None of the states were found to have a credit comparable to the credit this bill would allow.

### FISCAL IMPACT

The department's costs to implement this bill have yet to be determined. As the bill moves 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

This bill would result in the following revenue loss:

Estimated Revenue Impact of AB 1329 As Introduced February 27, 2015 Assumed Enactment After June 30, 2015 (\$ in Millions)		
2015-16	2016-17	2017-18
\$0	- \$390	- \$400

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

#### Revenue Discussion

This estimate is based on 2010 Census housing data, current Cal Fire data on cities with Very High Fire Hazard Severity (VHFHS) zones, and recent local fire district reporting. Based on this data, it is estimated that there are 4.8 million structures in counties or cities where there are Hazardous Fire Areas or designated VHFHS zones. Data suggests that of these, there would be

675,000 residential or business structures in Hazardous Fire Areas or VHFHS zones in 2016 subject to defensible space requirements that may qualify for this credit. It is assumed that annually 74 percent of these properties would have costs for either full fuel management activities to bring their properties in compliance or for lesser maintenance costs to keep these properties in compliance.

Research indicates the average professional fire protection project costs are approximately \$3,800 per year. At 25 percent of allowable costs, the average credit is calculated at \$950 per property for total credits of \$477 million in 2016. It was assumed that 85 percent of the credit would be used to offset current tax liabilities in the year generated and the remaining 15 percent would remain unclaimed. It is further assumed that 10 percent of those who file would be business entities subject to the PITL and would not be allowed the expense deduction, resulting in a deduction offset of approximately \$12 million for a net revenue loss of \$393 million for taxable year.

The tax-year estimates were converted to fiscal-year estimates and rounded to arrive at the amounts reflected in the table above.

### **SUPPORT/OPPOSITION**

Support: None provided.

Opposition: None provided.

### **ARGUMENTS**

Proponents: Some may argue that this bill would provide a credit that would encourage taxpayers to take much needed safety precautions to protect their property from wildfires.

Opponents: Some may argue that this bill would provide a credit for a safety area that is too narrow and may inadvertently exclude other safety concerns within the state that need assistance.

### **POLICY CONCERNS**

This bill would allow a tax credit for expenditures for creating the defensible space required by existing state law.<sup>7</sup>

It appears that the bill would preclude a taxpayer that creates a defensible space themselves (and does not hire help) from taking the credit. If this is contrary to the author's intent, the bill should be amended.

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

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<sup>7</sup> In January 2005, California Public Resources Code section 4291 became effective, thereby extending the defensible space clearance around homes and structures from 30 feet to 100 feet.

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.

#### **LEGISLATIVE STAFF CONTACT**

Jessica Deitchman  
Legislative Analyst, FTB  
(916) 845-6310

[jessica.deitchman@ftb.ca.gov](mailto:jessica.deitchman@ftb.ca.gov)

Jame Eiserman  
Revenue Manager, FTB  
(916) 845-7484

[jame.eiserman@ftb.ca.gov](mailto:jame.eiserman@ftb.ca.gov)

Gail Hall  
Legislative Director, FTB  
(916) 845-6333

[gail.hall@ftb.ca.gov](mailto:gail.hall@ftb.ca.gov)