Franchise Tax Board

ANALYSIS OF AMENDED BILL

Author:	Calderon	Analyst:	Diane Deatherage	Bill Number:	AB 1710
Related Bills:	See Legislative History	Telephone:	845-4783	Amended Date:	April 5, 2016
		Attorney:	Bruce Langston	Sponsor	

SUBJECT: Near-Zero-Emission or Zero-Emission Vehicle Credit and Deduction/FTB Report to Legislature Annually Regarding Efficacy of the Credit

SUMMARY

This bill would, under the Personal Income Tax Law (PITL), allow for a tax credit or a deduction for purchasing a near-zero-emission or zero-emission vehicle.

This analysis only addresses the provisions of the bill that would impact the department's programs and operations.

RECOMMENDATION

No position.

Summary of Amendments

The April 5, 2016, amendments removed provisions of the bill that would have modified the Health and Safety Code, relating to vehicular air pollution, and replaced them 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 promote near-zero-emission and zero-emission vehicle deployment in disadvantaged California communities, to drastically increase the use of those vehicles, and to meet specified goals established by the Governor and the Legislature.

EFFECTIVE/OPERATIVE DATE

This bill would be effective January 1, 2017, and specifically operative for taxable years beginning on or after January 1, 2017, and before January 1, 2026.

PROGRAM BACKGROUND

The Center for Sustainable Energy administers the Clean Vehicle Rebate Program (Rebate Program)[1] throughout the state for the California Air Resources Board.

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[1] This program was created in 2014 with the enactment of the Charge Ahead California Initiative (Health and Safety Code sections 44258 - 44258.5).

The Rebate Program promotes clean vehicle adoption by offering rebates of up to $6,500 for the purchase or lease of new, eligible zero-emission vehicles, including electric, plug-in hybrid electric, and fuel cell vehicles.

The Air Resources Board recently approved a funding plan that included an income cap for higher-income consumers and increased rebate levels for low- and moderate-income consumers participating in the Rebate Program, effective for rebate applications for vehicles purchased or leased on or after March 29, 2016.

FEDERAL/STATE LAW

General Deductions and Credits

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. Under Revenue and Taxation Code (R&TC) section 41, legislation that would create a new tax credit is required to include specific goals, purposes, objectives, and performance measures to allow the Legislature to evaluate the credit's effectiveness.

Credits for Plug-in Electric Drive Motor Vehicles

Federal law provides a credit for Qualified Plug-in Electric Drive Motor Vehicles, including passenger vehicles and light trucks.

The credit is equal to $2,500, plus, for a vehicle which draws propulsion energy from a battery with at least 5 kilowatt hours of capacity, $417, plus an additional $417 for each kilowatt hour of battery capacity in excess of 5 kilowatt hours. The total amount of the credit allowed for a vehicle is limited to $7,500.

The vehicles must be acquired by a taxpayer for use or lease[2] and not for resale. Additionally, the original use of the vehicle must commence with the taxpayer and the vehicle must be used predominantly in the United States. For purposes of the credit, a vehicle is not considered acquired prior to the time when title to the vehicle passes to the taxpayer under state law.

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[2] In the case of an operating lease, only the lessor may claim the credit.

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

THIS BILL

Under the PITL, for each taxable year beginning on or after January 1, 2017, and before January 1, 2026, a qualified taxpayer would be allowed a tax credit in an amount equal to $2,500.

Under the PITL, for taxable years beginning on or after January 1, 2017, and before January 1, 2026, a qualified taxpayer, who purchased a near-zero-emission or zero-emission vehicle, would be allowed as an "above-the-line" deduction[3] in an amount equal to $2,500.

A qualified taxpayer would be required to make an irrevocable election to claim the credit in lieu of the above-the-line deduction or to claim the above-the-line deduction in lieu of the credit.

The bill would define the following phrases:

- For determining the tax credit, "qualified taxpayer" would mean an individual or individuals who meet the income eligibility requirements specified by the State Air Resources Board and who purchased a near-zero or zero-emission vehicle during the taxable year.

- For determining the above-the-line deduction, "qualified taxpayer" would mean an individual or individuals who meet the income eligibility requirements specified by the State Air Resources Board.

- "Near-zero-emission vehicle" would mean a vehicle that utilizes zero-emission technologies, enables technologies that provide a pathway to zero-emissions operations, or incorporates other technologies that significantly reduce criteria pollutants, toxic air contaminants, and greenhouse gas emissions, as defined by the State Air Resources Board in consultation with the State Energy Resources Conservation and Development Commission consistent with meeting the state's mid- and long-term air quality standards and climate goals.

- "Zero-emission vehicle" would mean a vehicle that produces no emissions of criteria pollutants, toxic air contaminants, and greenhouse gases when stationary or operating, as determined by the State Air Resources Board.

The bill would also allow any unused credit to be carried forward for seven years.

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[3] A deduction that reduces gross income to arrive at adjusted gross income, before the itemized or standard deduction.

This bill contains language that it is the intent of the Legislature to enact legislation to provide that the credit would be refundable, upon appropriation, if the amount of the credit exceeds the taxpayer's net tax, in lieu of the credit carry forward.

The department, in consultation with the State Board of Equalization, would be required to report regarding the efficacy of the exemption, credit, and deduction to the Legislature by January 1, 2018, and annually each January 1, thereafter until January 1, 2027.

The tax credit and deduction provisions would remain in effect until December 1, 2026, and as of that date would be repealed.

IMPLEMENTATION CONSIDERATIONS

Department staff has identified the following implementation considerations for purposes of a high-level discussion; additional considerations may be identified as the bill moves through the legislative process. Department staff is available to work with the author's office to resolve these and other considerations that may be identified.

The bill would allow the credit or deduction irrespective of the vehicle's purchase price. A qualified taxpayer would be able to purchase a used vehicle for less than $2,500 and still receive a credit or deduction of $2,500. If this is contrary to the author's intent, the bill should be amended.

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.

This bill has unparallel language in the definition of a "qualified taxpayer." The different definitions could lead to disputes with taxpayers and would complicate the administration of this bill. The author may want to amend the bill to make the definitions the same.

The "qualified taxpayer" definitions lack language that would limit the credit or deduction to low- and moderate-income taxpayers. If this is contrary to the author's intent, the bill should be amended.

It is unclear in the "near-zero-emission vehicle" definition which vehicles would qualify for the credit or deduction as defined by the State Air Resources Board in consultation with the State Energy Resources Conservation and Development Commission. The uncertainty of the definition could lead to disputes with taxpayers and would complicate the administration of this bill. The bill should be amended to clarify the definition.

This bill lacks administrative details necessary to implement the bill and determine its impacts to the department's systems, forms, and processes. The bill is silent or unclear on the following issues:

- Because the bill fails to state otherwise, a vehicle purchased and used outside the state could generate the tax benefit this bill would establish. If this is contrary to the author's intent, the bill should be amended.

- Because the bill fails to specify otherwise, the benefit would apply to new, leased, and used vehicles; if this is contrary to the author's intent, the bill should be amended.

- Because the bill fails to specify otherwise, each sale of a vehicle to an otherwise qualified taxpayer would generate an additional tax benefit regardless of the length of time each qualified taxpayer held title to the vehicle. The author may wish to amend the bill to specify how long the taxpayer must retain the vehicle title.

- The bill lacks language relating to the irrevocable election made by the taxpayer that is needed for administrative ease and to alleviate taxpayer confusion.

TECHNICAL CONSIDERATIONS

Although the bill contains language that it is the Legislature's intent to enact legislation to provide a refundable credit, the bill lacks the specific language necessary for a refundable credit.

LEGISLATIVE HISTORY

AB 998 (Kelley, 2001/2002) would have allowed a credit of 30 percent of the purchase price of a new zero-emission Neighborhood Electric Vehicle. AB 998 failed to pass out of the Assembly by the constitutional deadline.

SB 1726 (Burton, 1999/2000) would have allowed a credit of up to $3,000 for each zero-emission vehicle leased or purchased. SB 1726 failed to pass out of the Senate 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.

Florida does not have a personal income tax.

None of these states provide a credit or deduction comparable to the one proposed by this bill.

FISCAL IMPACT

The department's costs to implement this bill have yet to be determined. As the bill moves through the legislative process, 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 1710* As Amended April 5, 2016 Assumed Enactment After June 30, 2016 ($ in Millions)		
2016-17	2017-18	2018-19
- $55	- $120	- $160

* The estimated impact of the deduction is less than 1 percent of the estimate shown in the table above.

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

Revenue Discussion

Based on available electric vehicles sales data, it is estimated that approximately 75,000 qualified new and used vehicles would be purchased by qualified taxpayers in 2017. It is estimated that 85 percent, or 65,000, would be purchased by qualified taxpayers who have taxable income. It is further assumed that in the year the taxpayer purchases the vehicle, 95 percent would elect to claim the credit and the remaining 5 percent would choose to claim the above-the-line deduction. It is assumed that 10,000 vehicles purchased by taxpayers who do not have taxable income, would choose to take the deduction and carryover the losses into future years.

For those who claim the $2,500 credit, the credit generated is estimated to be $150 million. It is assumed that 60 percent of the credit will be claimed in the year generated and the remaining 40 percent would be used over the next 6 years. This results in an estimated loss of $92 million in 2017. It is estimated that for those who claim the $2,500 deduction, taxable income would be reduced by $8 million in 2017. Using an average tax rate of 4 percent, the estimated loss from the deductions would be $325,000 in 2017.

The combined estimated revenue loss is $92 million (rounded). The estimate is then adjusted to reflect changes in the economy over time. The tax-year estimates are converted to fiscal-year estimates, and then rounded to arrive at the estimates shown in the above table.

SUPPORT/OPPOSITION

Support: CALSTART, Alta Motors, Association of Global Automakers, Sierra Club California, and Alliance of Automobile Manufacturers.

Opposition: None provided.

ARGUMENTS

Proponents: Some may argue that the bill would assist in reducing pollution in California by encouraging taxpayers to purchase near-zero-emission or zero-emission vehicles.

Opponents: Some may argue that air pollution is a critical state interest and should be more robustly encouraged by expanding the credit to include more vehicles.

POLICY CONCERNS

This bill would create differences between federal and California tax law, thereby increasing the complexity of California tax return preparation.

The bill lacks a requirement for the vehicle to be registered or operated in California.

Conflicting tax policies come into play whenever a credit is provided for an item that is already deductible as a business expense or is depreciable. Providing both a credit and allowing the full amount to be deducted would have the effect of providing a double benefit for that item (in addition to the sales tax exemption provided by this bill). On the other hand, making an adjustment to reduce basis in order to eliminate the double benefit creates a difference between state and federal taxable income, which is contrary to the state's general federal conformity policy. In the case of a one-time business expense deduction, the reduction of that expense by the amount of the credit would not create an ongoing depreciation difference.

This bill fails to limit the amount of the credit that may be taken. Credits that could potentially be quite costly are sometimes limited either on a per-project or per-taxpayer basis. This bill would allow a taxpayer to receive credits on an unlimited number of vehicles.

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