Franchise Tax Board

SUMMARY ANALYSIS OF AMENDED BILL

Author:	Nazarian	Analyst:	Jessica Deitchman	Bill Number:	AB 428
Related Bills:	See Prior Analysis	Telephone:	845-6310	Amended Date:	June 17, 2015
		Attorney:	Bruce Langston	Sponsor	

SUBJECT:	Seismic Retrofit of At-Risk Property Credit

SUMMARY

This bill would, under the Personal Income Tax Law (PITL) and Corporation Tax Law (CTL), allow a credit for costs to seismically retrofit “at-risk” buildings.

RECOMMENDATION

No position.

SUMMARY OF AMENDMENTS

The June 17, 2015, amendments added provisions to clarify how a taxpayer would receive certification for seismic retrofit construction, added provisions clarifying the certification process, revised the operative and sunset dates, and added an annual cap on the amount of credit that could be allocated.

As a result of these amendments, the “This Bill,” “Effective/Operative Date,” “Fiscal Impact” and “Economic Impact” sections as provided in the department’s analysis of the bill as amended May 21, 2015, have been revised, and a “Technical Consideration” has been identified. The remainder of that analysis still applies. The “Support/Opposition” and “Implementation Consideration” sections have been restated for convenience.

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, 2017, and before January 1, 2022.

THIS BILL

For taxable years beginning on or after January 1, 2017, and before January 1, 2022, this bill would allow a qualified taxpayer a credit in an amount equal to 30 percent of the qualified taxpayer’s qualified costs.

The bill would define the following phrases:

- “At-risk property” means a building that is deemed hazardous and in danger of collapse in the event of a catastrophic earthquake, including, but not limited to, soft story buildings, nonductile concrete residential buildings, and pre-1994 concrete residential buildings.

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- "Qualified building" means a building that has been certified as an at-risk property. A qualified building includes a mobilehome registered by the Department of Housing and Community Development.
- "Qualified costs" means the costs paid or incurred by the taxpayer for any completed seismic retrofit construction on a qualified building, including any engineering or architectural design work necessary to permit or complete the seismic retrofit construction and does not include any of the following costs paid or incurred by the qualified taxpayer:
  - Maintenance, including abatement of deferred or inadequate maintenance, and correction of violations unrelated to the seismic retrofit construction.
  - Repair, including repair of earthquake damage.
  - Seismic retrofit construction required by local building codes as a result of addition, repair, building relocation, change of use, or occupancy.
  - Other work or improvement required by local building or planning codes as a result of the intended seismic retrofit construction.
  - Rent reductions or other associated compensation, compliance actions, or other related coordination involving the qualified taxpayer and any other party, including a tenant, insurer, or lender.
  - Replacement of existing building components, including equipment, except as needed to complete the seismic retrofit construction.
  - Bracing or securing nonpermanent building contents.
  - The offset of costs, reimbursements, or other costs transferred from the qualified taxpayer to others.
  - Any amount paid by the qualified taxpayer to the jurisdiction with authority for building code enforcement for issuing the certifications required.
- "Qualified taxpayer" means a taxpayer that is an owner of a qualified building located in this state. A taxpayer that owns a proportional share of a qualified building in this state may claim the credit allowed by this bill based on the taxpayer's share of the qualified costs.
- "Seismic retrofit construction" means alteration of a qualified building or its components to substantially mitigate seismic damage. Seismic retrofit construction would be for work performed, and for which qualified costs were paid or incurred, on or after January 1, 2017. Seismic retrofit construction would include, but not be limited to, the following:
  - Anchoring the structure to the foundation.
  - Bracing cripple walls.
  - Bracing hot water heaters.
  - Installing automatic gas shutoff valves.
  - Repairing or reinforcing the foundation to improve the integrity of the foundation against seismic damage.
  - Anchoring fuel storage.

- Installing earthquake-resistant bracing system for mobilehomes that are registered with the California Department of Housing and Community Development.

Seismic retrofit construction would not include construction performed to bring a building into compliance with local building codes.

To be eligible for the credit, the following must apply:

The qualified taxpayer would be required to do all of the following:

- Prior to the seismic retrofit construction, obtain certification from the appropriate jurisdiction with local building code enforcement authority that the building is an “at-risk property”.
- Obtain certification from the appropriate jurisdiction with authority for building code enforcement, upon a review of the building, that the completed construction satisfies the definition of seismic retrofit construction. The certification would identify what part of the completed construction, if any, is not seismic retrofit construction and specify a dollar amount of qualified costs.
- Request and be granted an allocation of the credit from the Franchise Tax Board (FTB). To request an allocation, the taxpayer must sign and submit to the FTB an application to receive credit for the retrofit construction and provide a copy of the certification. Upon receipt of the application and certification, the FTB shall notify the taxpayer of the amount, if any, of credit allocated.
- Retain for his or her records a copy of the certifications.

The jurisdiction with authority for building code enforcement in which a qualified building is located has entered into an agreement with the state to provide certifications and to not seek reimbursement pursuant to Section 6 of Article XIII B of the California Constitution for any costs incurred in providing those certifications.

The qualified taxpayer would be required to claim one-fifth of the credit amount for the taxable year in which the credit is allocated and one-fifth of the credit amount for each of the subsequent four taxable years.

The qualified costs used to calculate the credit would be reduced by any grant provided by a public entity for the seismic retrofit construction.

This bill would allow unused credits to be carried over for up to five years, if necessary.

The total amount of credit that may be allocated could not exceed the sum of the following:

- $12,000,000 for the 2017 calendar year and each calendar year thereafter.
- The amount of previously unallocated credits allowed.

Upon receipt of the application and certification, the FTB would notify the taxpayer of the amount of credit allowed, if any, and allocate the credit to the taxpayer on a first-come-first-served basis.

The taxpayer must claim the credit on a timely-filed original return.

The determination of the FTB with respect to the allocation of the credit, and whether a return has been timely filed may not be reviewed in any administrative or judicial proceeding.

Any disallowance of a credit claimed due to a determination, including the application of the limitation of $12,000,000 per calendar year, would be treated as a mathematical error appearing on the return. Any amount of tax resulting from that disallowance may be assessed by the FTB in the same manner as provided by Section 19051.

This credit would be in lieu of any other credit or deduction that the qualified taxpayer may otherwise claim under the PITL and CTL with respect to qualified costs.

The FTB may prescribe rules, guidelines, or procedures necessary or appropriate to carry out the purposes of this bill, including any guidelines regarding the allocation of the credit allowed. The rules, guidelines or procedures would be exempt from the Administrative Procedure Act.

This credit would remain in effect only until December 1, 2022, and as of that date is repealed.

The bill provides that the provisions of Revenue and Taxation Code (R&TC) section 41[1] would not apply.

IMPLEMENTATION CONSIDERATIONS

Implementing this bill would require some changes to existing tax forms and instructions and information systems.

TECHNICAL CONSIDERATIONS

For clarity on when a credit can be claimed, the following amendment is recommended:

On page 5, line 5 and on page 8, line 36 strikeout “allowed” and insert “allocated”

FISCAL IMPACT

Staff estimates a cost of approximately $254,727 in fiscal year 2015/2016 and ongoing costs of $128,000 to develop and administer an allocation process, program systems, and test revisions to existing systems for this bill. The department will pursue a budget change proposal if necessary.

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[1] R&TC section 41 requires any bill introduced on or after January 1, 2015, that creates a new tax credit to contain language specifying goals, purposes, objectives, performance measures, and data collection and reporting requirements.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of AB 428 As Amended June 17, 2015 Assumed Enactment After June 30, 2015 ($ in Millions)		
2016-17	2017-18	2018-19
- $0.7	- $2.7	- $4.6
This estimate assumes that there will be no new mandates requiring retrofitting activities anywhere in the state. The costs could increase significantly if a state-wide mandate is put in place.		

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

Revenue Discussion:

This bill would establish a credit for qualified costs incurred for seismic retrofit construction on an at-risk building. The maximum credit allocation would be capped at $12 million per calendar year. Based on discussions with industry experts and 2013 U.S. Census data on buildings in earthquake areas it is estimated that approximately 2,150 buildings would undergo retrofitting each year. Data provided by the California Seismic Safety Commission indicated the retrofitting cost is approximately $20,000 for residential housing, $10,000 for mobile homes, and $100,000 for commercial buildings. This data results in an estimated $83 million dollars in retrofitting costs for 2013. The estimate was grown for inflation to $89 million in qualified expenditures for 2017. The amount of estimated qualified expenses was then reduced by the estimated amount of retrofitting grants issued annually (estimated at $10 million annually). This resulted in $79 million in qualified retrofitting costs incurred for 2017.

The credit is equal to 30 percent of qualified costs. This results in approximately $24 million in credit generated in 2017. This credit amount exceeds the $12 million maximum credit allocation for 2017 and, therefore, the total qualifying credit for 2017 would be $12 million. The same is true for subsequent years resulting in $12 million of credits for those years The credit must be taken evenly over 5 years, resulting in $2.4 million available in tax year 2017. The credit available will peak, when there is a five combined year period, in 2021 at $12 million. Experience shows that 70 percent of the available credit will be used in the year the credit is generated and the remaining 30 percent of the credit will be used over the subsequent four years. This results in an estimated credit usage beginning at approximately $1.7 million in taxable year 2017 and peaking in 2021 at approximately $10.6 million. An adjustment was made to reflect the decreased depreciation deduction allowed when the credit is claimed.

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

SUPPORT/OPPOSITION[2]

Support: California Apartment Association and Western Manufactured Housing Communities Association.

Opposition: None provided.

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[2] As provided in the Assembly Revenue & Taxation Committee analysis dated May 15, 2015.