



## Bill Analysis

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Sponsor:

Bill Number: SB 1410

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Amended: June 16, 2020,

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Related Bills: See Legislative  
History

and June 19, 2020

## SUBJECT

Tenant-Owner COVID-19 Eviction Relief Agreements and Related Tax Credit

## SUMMARY

This bill, under the Personal Income Tax Law (PITL), the Corporation Tax Law (CTL), the Code of Civil Procedure, and the Civil Code, would allow tenants and property owners to enter into a tenant-owner COVID-19 eviction relief agreement (eviction relief agreement) to allow rents by the tenant to be deferred during the COVID-19 state of emergency plus an unspecified number of days.

This bill would do the following:

- Allow for rent deferral pursuant to eviction relief agreements for tenants.
- Create a COVID-19 eviction relief agreement tax credit for landlords.

## RECOMMENDATION

No position.

## SUMMARY OF AMENDMENTS

The June 16, 2020, amendments removed provisions of the bill related to the Health and Safety Code, and replaced them with provisions related to the Civil Code and the provisions discussed in this analysis.

The June 19, 2020, amendments changed the name of agreements to COVID-19 eviction relief agreements, removed an urgency clause, and made the credit refundable upon appropriation by the Legislature.

This analysis only addresses the provisions that would impact the department.

## REASON FOR THE BILL

The reason for this bill is to assist tenants and owners of residential real property or mobilehome parks during the state of emergency related to the COVID-19 pandemic.

*COVID-19 Eviction Relief Provisions (Bill sections 1, 2, 4, 5 and 7)*

For taxable years beginning on or after January 1, 2024, and before January 1, 2034, the bill would require a tenant to pay rent deferred under an eviction relief agreement, without interest, in equal installments over a period of ten years in taxable years beginning on or after January 1, 2024, and before January 1, 2034. In addition, the bill would require tenants to include installment payments due in the tax return filed for each year. Each year, tenants may apply for reduction or exemption from the installment payment due for that year.

Reduction or exemption of an installment payment would be based on a taxpayer's taxable income for that year, as follows:

- A. For individuals with an income equal to or greater than 150 percent of the median state income, 100 percent of the installment payment.<sup>1</sup>
- B. For individuals with an income between 100 and 149 percent, inclusive, of the median state income, 75 percent of the installment payment.
- C. For individuals with an income between 75 and 99 percent, inclusive, of the median state income, 50 percent of the installment payment.
- D. For individuals with less than 75 percent of the median state income, none of the installment payment.

For purposes of this provision, the following definitions apply:

- 1. "Median state income" means the median state income provided by the Department of Finance.
- 2. "Tenant" means a tenant who signs and executes a COVID-19 eviction agreement with the owner of real property.
- 3. "Owner of real property" means an owner of residential real property or an owner of a mobilehome park.
- 4. "Rent" does not include rental assistance payments from any federal or state governmental source or a nonprofit organization received by the tenant or by the owner of real property on the tenant's behalf.
- 5. "State of emergency" means an emergency related to the COVID-19 pandemic declared by the Governor pursuant to the California Emergency Services Act (Chapter 7 (commencing with Section 8550) of Division 1 of Title 2 of the Government Code).

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<sup>1</sup> As written, this would remove 100 percent of the amount due even though income is 150 percent above median income. We have noted this as a possible technical amendment below.

The bill would allow the Franchise Tax Board (FTB) to specify the form and manner of a request for reduction or elimination of an installment payment. The bill would preclude the FTB or any other person from collecting any portion of the installment payments that are allowed to be reduced or forgiven. Subsequent annual installments would remain due unless reduced or forgiven by the FTB. In addition, the amount of unpaid rent reduced or forgiven, while recognized as cancellation of indebtedness income by definition, would be excluded from the taxpayer's California gross income.

In addition, the bill authorizes the FTB to require any person required to withhold under Revenue and Taxation Code (R&TC) section 18662, which generally applies to withholding at source for out-of-state taxpayers with California source income, installment payments and transmit them to the FTB. The bill would also authorize the FTB to collect installment payments in any manner authorized for the collection of delinquent income tax liabilities, including, but not limited to liens, levies, and wage garnishment. The bill would require the FTB to transfer moneys collected under this bill to the Treasurer to be deposited in the General Fund.

Upon registering with the FTB, owners of real property who execute an eviction relief agreement with a tenant who is not a related party would be eligible for a tax credit (discussed below). If the owner violates the eviction relief agreement, the owner would be required to repay the credit to the FTB immediately, plus interest from the date the credit was first claimed on the tax return.

Owners of real property would be required to provide the FTB with a copy of the eviction relief agreement and a copy of the signed receipt of acknowledgment from the tenant, in a form and manner specified by the FTB, by the following dates:

- For agreements executed on or before January 1, 2021, no later than January 1, 2021.
- For agreements executed on or after January 1, 2021, no later than 60 days after the date the agreement is signed by both the owner and the tenant.

Owners of real property would be required to provide a copy of the eviction relief agreement to the tenant within five days from when the agreement is executed.

The bill would require the FTB to create a form "tenant-owner COVID-19 eviction relief agreement" and accompanying notice in English, Spanish, Chinese, Tagalog, Vietnamese, and Korean. The FTB would be required to make the agreement and notice available on its website within 30 days of the operative date of the R&TC section 19543. The bill would allow the FTB to request assistance from other state agencies or public entities for translation of the agreement and notice.

The bill includes an eviction relief agreement and accompanying notice that an owner of real property, as defined, would be required to provide to the tenant along with the signed agreement to the tenant before they could enter into an eviction relief agreement.

If an owner makes an offer to execute an eviction relief agreement to a tenant and the tenant rejects the offer, the owner must obtain a signed acknowledgment of receipt from the tenant. If a tenant does not respond to the offer or to the acknowledgment of receipt of the offer, the offer would be deemed rejected within 30 days of the owner hand-delivering the offer, or within 40 days of the owner mailing the offer and acknowledgment of receipt. If an offer is rejected, or deemed rejected, the owner would be permitted to file for eviction for nonpayment of rent during the state of emergency and an unspecified period after.

The bill would also allow an owner to evict a tenant for the same period if the tenant has destroyed property or engaged in behavior that creates a substantial threat to the public health or safety even if the tenant agreed to an eviction relief agreement.

Each owner would be required to have their own agreement with a tenant. If there is more than one tenant on one lease agreement for the unit, each tenant would be required to have a separate eviction relief agreement with the owner. If there is more than one tenant for the unit and each tenant has a separate lease agreement, each tenant would also be required to have an eviction relief agreement with the owner of real property.

The bill states that it is the intent of the Legislature that the prohibition against eviction for unpaid rent during the state of emergency and unspecified period after will apply retroactively. The bill specifies that the evictions for unpaid rent pursuant to a rejected eviction relief agreement would be allowed prospectively.

The provisions relating to eviction would remain in effect for two years after the state of emergency related to the COVID-19 pandemic terminates, and as of that date would be repealed. The provisions regarding eviction relief agreements and repayment of deferred rent would remain in effect until December 31, 2034, and as of that date would be repealed.

*COVID-19 Eviction Agreement Tax Credit Provisions (Bill sections 3 and 6)*

For each taxable year beginning on or after January 1, 2024, and before January 1, 2034, this bill would allow a credit against the "net tax," as defined in R&TC section 17039, to a qualified taxpayer in an amount equal to the amount of qualified rent deferred by the qualified taxpayer. In addition, if the qualified taxpayer is also a small business owner, as defined, the credit would be an amount equal to the amount of qualified rent deferred by the qualified taxpayer, plus an adjustment for inflation no less than 2 percent. The bill would disallow any credit or deduction

otherwise allowed under the PITL or CTL for amounts paid or incurred by the taxpayer upon which this credit is based.

The bill provides that "qualified rent" would mean an amount equal to the gross amount of unpaid rent deferred by the qualified taxpayer in a signed and executed eviction relief agreement between the qualified taxpayer and the tenant that meets the requirements of Section 1947.20 of the Civil Code, relating to eviction relief agreements. Qualified rent would not include any amounts in excess of 100 percent of the sum of the amounts of rent charged per month as stated in the lease agreement that would have been paid but for the eviction relief agreement for those months in which the eviction relief agreement applies.

In addition, the bill defines "qualified taxpayer" as an owner of residential real property or a mobilehome park, that is subject to Chapter 2 (commencing with Section 1940) of Title 5 of Part 4 of Division 3 of the Civil Code, and has registered with the FTB and been allowed a credit. For pass-thru entities, the determination of whether a taxpayer is a qualified taxpayer under this section will be made at the entity level and any credit under this section is not allowed to the pass-thru entity, but will be passed through to the partners or shareholders under the PITL and CTL. "Pass-thru entity" would mean any entity taxed as a partnership or "S" corporation.

"Small business owner" would mean an individual that is the sole owner, or owners in the case of those individuals that are married and filing a joint return for the property, and whose state adjusted gross income is no more than \$1,000,000 for the taxable year in which the eviction relief agreement was executed.

On or before January 1, 2021, the FTB would be required to create a registration program for qualified taxpayers. The registration form would be required to include, but not be limited to:

- Name under which the qualified taxpayer transacts or intends to transact business.
- Name, address, and social security number or tax identification number of the tenant or tenants.
- Start date of the rent deferral, and the amount of rent deferred.
- The location of the qualified taxpayer's place or places of business.
- A copy or copies of the executed eviction relief agreements.
- A copy or copies of the existing lease agreements between the qualified taxpayer and the tenant or tenants.

The FTB would be required to approve a reservation with respect to a qualified taxpayer upon receipt of the registration form and provide notice to the taxpayer including the amount of the credit that would be available if the eviction relief agreement is completed. A qualified taxpayer may choose to claim the credit in any

taxable year beginning on or after January 1, 2024, and before January 1, 2034. If the credit exceeds the qualified taxpayer's liability, the excess could, at the qualified taxpayer's choosing, either be refunded (upon appropriation by the Legislature) or carried over to subsequent tax years until exhausted. In addition, a qualified taxpayer would have the ability to sell the credit to no more than one taxpayer, who must be an unrelated party, and the credit could not be resold. The buyer could use the purchased tax credit for taxable years beginning on or after January 1, 2024, and before January 1, 2034. A qualified taxpayer would not be allowed to assign or sell any tax credit if the tax credit is claimed on any tax return of the qualified taxpayer.

The bill requires the FTB to develop a tax form to be used by the qualified taxpayer to verify the amount of qualified rent deferred pursuant to an executed eviction relief agreement.

The bill would require the FTB, beginning January 1, 2022, and annually thereafter, to determine the aggregate amount of credit that has been approved for each calendar year.

The bill grants FTB emergency regulatory authority to prescribe any regulations necessary or appropriate to administer the credit, including any regulations to prevent improper claims from being filed or improper payments from being made with respect to net earnings from self-employment.

#### *Effective/Operative Date*

If enacted on or before September 30, 2020, this bill would be effective and operative on January 1, 2021.

#### *Federal/State Law*

Gross income, defined by Internal Revenue Code section 61, which California generally follows under R&TC sections 17071 and 24271, is broadly defined, and generally consists of all income from all sources, such as compensation for services, business income, interest, rents, dividends, and gains from the sale of property. Only items that are specifically exempt may be excluded from gross income.

Generally, if a debt owed by a taxpayer is canceled or forgiven, other than as a gift or bequest, the taxpayer must include the canceled amount in income. There are certain exceptions to this, such as when a taxpayer is insolvent.

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 hiring credits). These credits generally are designed to provide incentives for taxpayers to perform various actions or activities that they may not otherwise undertake.

There are currently no federal or state credits comparable to the credit this bill would create.

### *Estimated Volumes*

FTB records indicate there are approximately 3.7 million residential renters in California. Presuming this rent deferral is focused on those with financial difficulties, even though not statutorily noted, the FTB would estimate approximately 600,000 tenants would participate, involving properties owned by approximately 350,000 landlords.

### *Implementation Considerations*

Statutory language indicates a large portion of work would be needed in the first four to six month of 2021. With the large estimated volumes, work would be substantial. The FTB does not currently have the capacity to take on this program and cannot stand up this program as intended in the time frame desired. The FTB does not have the resources to implement before January 1, 2021, without significant impacts and risks to systems and core processes, such as return/payment processing. The FTB would need assistance from external partners to determine how this substantial work could be accomplished in such a short time, considering the program itself and the additional duration of hiring, training, and procurement processes.

### *Technical Considerations*

There are numerous items needing clarity within the bill to ensure the program can be administered as intended and the bill produces the desired outcome. Department staff is available to work with the author's office and can provide language to resolve these and other concerns that may be identified.

Some of these technical concerns include, but are not limited to:

- Deductibility of rental expenses if no income is reported.
- Whether modifications to agreements and/or early payments to pay off debt are permitted.
- Whether agreements can cover only deferred rents to date or project out future payments.
- For the sale of credits, are only full sales allowed or are partial sales permitted?
- Computational rules for the forgiveness of debt.
- Potential withholding rules for the deferred rent payments due, which can be sizable.
- Credit recapture rule mechanics.
- Treatment for out of state debtors.
- Collection rules related to offsets.

- What if the owner sells the credit and then it is violated? Or, what if it is violated and then sold? Is the purchaser protected? Is the owner taxed on the gain from the sale of credit?
- Would the renter's credit for a tenant getting relief still be available? If renters are paying rent in 2024 – 2034, do they get the renter's credit upon repayment?

### *Policy Concerns*

This could be a disincentive to pay rent by tenants who might otherwise pay rent or who would like to resume paying rent due to a change in their financial situation but this rent deferral agreement prevents that option.

Many property owners utilize monthly rent payments to cover expenses of the property such as mortgage payments, taxes, business staffing costs, utilities and general upkeep costs. Deferring the rental payment could result in the inability to pay these costs which could force the owner to sell the property or the property could be subject to foreclosure, which ultimately could reduce available rental units. As a result, tenants may also have fewer options for available housing.

It is unclear how these agreements impact evictions that are not rent-related (but still covered under the provisions) since there is no monetary basis upon which to compute a credit. Additionally, if presented with an agreement, a tenant only has the option to reject (i.e., effectively agreeing to allow eviction to continue) or sign the agreement but does not allow an "opt out" option without a potential consequence. Likewise, it is unclear in the language if a property owner can refuse to enter into an agreement requested by a tenant.

Taxpayers with rent deferred installment payments may now have to file for the first time as they otherwise may not have a filing requirement solely based on income.

For taxpayers who are granted debt forgiveness for the deferred rent, this might be required to be reported and subject to tax at the federal level, which creates a liability subject to payment and collection. This income could also be considered income when determining qualifications for various assistance programs.

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

This bill could potentially saturate the market with the availability of COVID-19 eviction relief agreement credits for sale. It may be hard for property owners with immediate cash flow needs to identify buyers for their credit. Additionally, if amended to a nonrefundable credit that a qualified taxpayer would be required to claim in equal installments over 10 years as suggested at the Senate Governance and Finance



Committee Hearing on June, 22, 2020, the credit may lose attractiveness in the market.

The proposed statute was recently amended to allow for the refundable portion of the credit to be claimed only if an appropriation occurs. Clear rules must be established to determine the priority of who receives credits, and to what extent, if the appropriation is insufficient to cover the refundable credits that are due and payable.

The removal of the urgency clause results in tenants and property owners not being able to enter into these agreements until January 1, 2021, which may thwart the intention of the legislation and lead to harm of either the tenant or owner.

### **LEGISLATIVE HISTORY**

AB 828 (Ting, et al., 2019/2020) would, under the Civil Code, the Code of Civil Procedure, and the Government Code, temporarily freeze foreclosures and unlawful detainer actions while there is a state or locally declared state of emergency related to COVID-19. In addition, this bill, under the R&TC, would suspend the sale of property tax-defaulted residential real property while there is a state or locally declared state of emergency related to COVID-19. AB 828 is currently in the committee process.

### **PROGRAM BACKGROUND**

None Noted.

### **FISCAL IMPACT**

This bill would require the implementation of a new program, which would require additional and significant resources, e.g., staff, new systems, new forms and instructions, taxpayer education and outreach. In addition, the FTB would need to develop a rent forgiveness program, track deferred rent payments and credit sales/reporting, and conduct collection action if necessary. This bill would significantly impact the department's programming and processing costs and potentially require a shift of resources from other workloads to meet the timeframes outlined in this bill, considering the potential volume of tenants and owners who may participate in this program.

As the bill continues to move through the legislative process, specific costs will be identified, but they are expected to be significant.

**ECONOMIC IMPACT**

*Revenue Estimate*

The following estimate is revised to include labor force data from the Bureau of Labor Statistics. Additional detail regarding the components of the estimate is included below.

This bill would result in the following revenue impact:

Revised Estimated Revenue Impact of SB 1410 as Amended June 19, 2020  
 Assumed Enactment after June 30, 2020

(\$ in Millions)

Fiscal Year	Loss of Tax Revenue due to Unpaid Rental Income	Loss of Revenue due to Refund of Credit*	Loss of Revenue due to Credit Offsetting Tax Liability	Gain of Revenue due to Payback of Deferred Rent	Revenue
2020-2021	-\$1,000	n/a	n/a	n/a	-\$1,000
2021-2022	-\$300	n/a	n/a	n/a	-\$300
2022-2023	-\$20	n/a	n/a	n/a	-\$20
2023-2024	n/a	-\$9,000	n/a	+\$500	-\$8,500
2024-2025	n/a	n/a	-\$8,500	+\$1,000	-\$7,500
2025-2026	n/a	n/a	-\$2,000	+\$1,000	-\$1,000
2026-2027 through 2033-2034	n/a	n/a	-\$2,800	+\$7,500	+\$4,700

\*For purposes of calculating the revenue impact, there is no distinguishing between whether credits are used to offset tax or whether they are refunded. The net impact to the general fund is the same. For purposes of this estimate, it is assumed that all refunds will be made in the first year available and that any remaining credits are those used to offset tax liability.

This analysis does not account for changes in employment, personal income, or gross state product that could result from this bill or for the net final payment method of accrual.

The revenue estimate assumes that an appropriation will be made each year that the bill is operative.

### *Revenue Discussion*

Using data from the FTB, the number of potentially qualified renters filing California tax returns in taxable year 2020 is estimated at 3.7 million. Using unemployment data from the Employment Development Department in conjunction with labor force data from the Bureau of Labor Statistics results in an unemployment rate of 22 percent. Applying this to the 3.7 million renters results in approximately 815,000 tenants in taxable year 2020 that will likely defer their rent. Multiplying the 815,000 tenants by the average rent of \$1,700, as indicated by the United States Census Bureau, results in a monthly rental income loss of \$1.4 billion. Applying an average tax rate of six percent, results in a revenue loss of approximately \$84 million per month. In addition, credits will be generated at \$1.4 billion per month to be used beginning in taxable year 2024. Credits have been assumed to be generated through June 30, 2021, for a total of \$22 billion of credits.

Of the \$22 billion credits generated, it is assumed that 50 percent, or \$11 billion, will be sold to an unrelated party and the remaining \$11 billion will be retained by the taxpayer that generated the credit.

In taxable year 2024, taxpayers that retained their credits will use approximately \$11 billion to either offset their tax liability or be refunded. Additionally, it is expected that another \$5 billion dollars of credits would be used to offset tax liability from taxpayer's who purchased credits in the prior years. The remainder of credits will be utilized over the next 6 years. This results in a total credit of \$16 billion used or refunded in the 2024 taxable year. This loss will be offset by \$1 billion as tenants begin to repay their rent.

Analysis of the expected taxable income of tenants indicates that 55 percent, or \$12 billion, of rent will not be repaid to the state because their taxable income allows them a reduction to, or elimination from, their installment payment as specified in the bill. The remaining \$10 billion of deferred rent will be repaid to the State in annual installments starting in the 2024 taxable year.

Approximately \$10 billion is expected to be repaid evenly over 10 years, or \$1 billion annually through taxable year 2033.

The tax year estimates are converted to fiscal year estimates, and then rounded to arrive at the amounts reflected in the above table.

## **LEGAL IMPACT**

None noted.

## **APPOINTMENTS**

None noted.

## **SUPPORT/OPPOSITION**

According to the June 23, 2020, Senate Floor Analyses of SB 1410, registered support for SB 1410 is unknown and registered opposition includes the California Association of Realtors and the California Rental Housing Association.

## **ARGUMENTS**

### *Arguments in Support*

According to the June 23, 2020, Senate Floor Analyses of SB 1410, " According to the author, 'in every part of California, there are families struggling financially because of COVID-19. Many are renters who are at risk of losing their home when emergency tenant protections run out. Many others are small landlords at risk of foreclosure because their tenants cannot afford to pay rent. SB 1410 will protect both categories of vulnerable Californians, providing renters and landlords with a voluntary path to stability. This bill does so responsibly, spacing out tenants' interest-free payments and landlords' corresponding tax credits over 10 years beginning in 2024, while providing for tenant hardship exemptions and the ability to sell landlords' tax credits. In doing so, this bill will protect the most vulnerable without sacrificing other programs supported by the State Budget.'"

### *Arguments in Opposition*

According to the June 23, 2020, Senate Floor Analyses of SB 1410, " According to the California Rental Housing Association, 'as drafted, we anticipate that almost any renter, regardless of ability to pay rent now, would force a housing provider to accept an agreement. The result will be a lack of income to rental housing providers, potentially increasing the likelihood of future foreclosures and a reduction in the rental housing stock because of rental housing providers choosing to leave the rental housing industry.'"

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