STATE OF CALIFORNIA
Franchise Tax Board

Bill Analysis

Author: Petrie-Norris

Sponsor:

Bill Number: AB 294

Related Bills: See Legislative History

Amended: April 12, 2023

SUBJECT

Gross Income Exclusion for Wildfire Damage

SUMMARY

The bill, under the Personal Income Tax Law (PITL) and the Corporation Tax Law (CTL), would provide a qualified taxpayer an exclusion from gross income for amounts received from a settlement entity for a wildfire.

RECOMMENDATION

No position.

SUMMARY OF AMENDMENTS

The April 12, 2023, amendments removed the words "natural disaster", added sunset and repeal dates, modified all the definitions, required the settlement entity to provide information to both the qualified taxpayer and the Franchise Tax Board (FTB), and added Revenue and Taxation Code (RTC) section 41 reporting requirements. This amendment resolved the implementation, technical, and policy considerations discussed in the FTB analysis of this bill as introduced on January 25, 2023, and created new technical considerations.

REASON FOR THE BILL

The reason for the bill is to prevent undue hardship for taxpayers who own real property, have a business, or reside, or resided, in parts of California devastated by a wildfire.

ANALYSIS

This bill, under the PITL and CTL, would provide an exclusion from gross income for any qualified amount received by a qualified taxpayer.

For purposes of the PITL and CTL, the following definitions would apply:

- "Qualified amount" means any amount received in settlement by a qualified taxpayer to replace property damaged or destroyed by wildfire if the property damaged or destroyed is located in an area of California damaged by the wildfire.
- "Qualified taxpayer" means any of the following:
    - Any taxpayer that owns real property located in an area damaged by a wildfire who paid or incurred expenses, and received amounts from a settlement, arising out of or pursuant to the wildfire.
    - Any taxpayer that has a place of business within an area damaged by a wildfire who paid or incurred expenses, and received amounts from a settlement, arising out of or pursuant to the wildfire.
- Under the PITL, a "qualified taxpayer" would also include any taxpayer that resides within an area damaged by a wildfire who paid or incurred expenses, and received amounts from a settlement, arising out of or pursuant to the wildfire.
- "Settlement entity" means the entity, approved by a class action settlement administrator, making the settlement payment to a qualified taxpayer. The settlement entity would be required to provide, upon request by the FTB or qualified taxpayer, documentation of the settlement payments in the form and manner requested by the FTB or the qualified taxpayer who may provide the documentation to the FTB upon request.

This bill would require the FTB to provide a written report to the Legislature by November 1, 2027, on the number of qualified taxpayers that excluded qualified amounts from gross income, and the aggregate amount of those settlement payments arising out of the wildfires and natural disasters.

This bill provides that the Section 41 reporting requirements would be treated as an exception to the general prohibition against disclosure of confidential taxpayer information.

The exclusion would be repealed on December 1, 2027.

Effective/Operative Date

This bill would be effective January 1, 2024, and operative for taxable years beginning on or after January 1, 2022, and before January 1, 2027.

Federal/State Law

Federal Law

Existing federal law, Internal Revenue Code (IRC) section 139, provides a general exclusion that gross income does not include any amount an individual receives as a qualified disaster payment. A qualified disaster payment means amounts paid to, or for the benefit of, an individual for several purposes, including to:

- Reimburse or pay reasonable and necessary personal, family, living, or funeral expenses the individual incurred because of a qualified disaster; or
- Reimburse or pay reasonable and necessary expenses the individual incurred for the repair or rehabilitation of a personal residence or repair or replacement of its contents, to the extent that the need for such repair, rehabilitation, or replacement is attributable to a qualified disaster.

For any federally declared disaster, an individual may exclude from income a valid disaster relief payment, which includes any amount the individual receives from the settlement award for a purpose listed above.

A qualified disaster includes any federally declared disaster, as defined in IRC section 165(i). A federally declared disaster is any disaster the President of the United States determines assistance from the federal government under the Robert T. Stafford Disaster Relief and Emergency Assistance Act is warranted. (The Federal Emergency Management Agency's website, www.fema.gov, provides the listing of federally declared disasters.)

State Law

California generally conforms to IRC section 139, as described above, and specifically allows an exclusion from gross income for:

- Settlement payments received from the Fire Victims Trust, and
- Settlement payments received from Southern California Edison for claims relating to the 2017 Thomas Fire or the 2018 Woolsey Fire.

Implementation Considerations

None noted.

Technical Considerations

For consistency of terminology, the following changes are recommended:

- In Section 17139(b)(1) and Section 24309.4(b)(1), the term “in settlement” should be replaced with “from a settlement entity.”
- In Section 17139(b)(2)(A), (B) and (C) and Section 24309.4(b)(2)(A) and (B), the term “settlement” should be replaced with “settlement entity.”
- In Section 17139(d)(1) and (2)(ii), remove the references to “natural disasters.”

Policy Considerations

None noted.

LEGISLATIVE HISTORY

SB 370 (McGuire, et al., 2023/2024) would allow an exclusion from gross income for amounts received in settlement for claims relating to the 2019 Kincade Fire and allow refunds of tax previously paid on those amounts. This bill is currently in the committee process.

SB 542 (Dahl and Dahl, 2023/2024) would provide a qualified taxpayer an exclusion from gross income for amounts received in settlement to replace property damaged or destroyed by the 2020 Zogg Fire.

AB 1249 (Gallagher, et al., Chapter 749, Statutes of 2022) provides an exclusion from gross income for amounts received in settlement under the order of the United States Bankruptcy Court for the Northern District of California dated June 20, 2020, case number 19-30088, docket number 8053.

SB 1246 (Stern, Chapter 841, Statutes of 2022) provides an exclusion from gross income for amounts received from Southern California Edison in settlement for claims relating to the 2017 Thomas Fire or the 2018 Woolsey Fire and allow refunds of tax previously paid on those amounts.

PROGRAM BACKGROUND

None noted.

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.

ECONOMIC IMPACT

Revenue Estimate

This proposal would allow a qualified taxpayer a gross income exclusion of qualified amounts received in settlement to replace property damaged or destroyed by wildfires. To calculate the revenue impact, the frequency of wildfires and the dollar amounts arising from settlement payouts from these wildfires must be known. Because it is difficult to predict the frequency of wildfires and the settlement amounts paid to qualified taxpayers, the revenue impact is unknown.

However, it is assumed that for every $1 million in settlement income received to replace property damaged or destroyed by wildfire and applying an average tax rate of 5 percent, the estimated revenue loss would be approximately $50,000.

LEGAL IMPACT

None noted.

APPOINTMENTS

None noted.

SUPPORT/OPPOSITION

As per the March 17, 2023, Assembly Committee on Revenue and Taxation analysis of AB 294, the following organizations are in support of this bill.

Support

California Apartment Association
California Farm Bureau Federation
Howard Jarvis Taxpayers Association

Opposition

None on file.

ARGUMENTS

As per the same analysis, the following argument in support of this bill was provided:

Proponents

According to The Howard Jarvis Taxpayers Association, "While some claims are already nontaxable under California law, real property (for victims who were insured), emotional distress, business loss and personal injury claims are taxable because they qualify as gross income. Over the last few years several bills, like SB 1246 (2022), AB 1249 (2022) and AB 50 (2011), have sought to address this issue by exempting settlements paid out related to specific incidents. AB 294 improves upon this by putting an end to the natural disaster whack-a-mole of previous legislation by stating, once and for all, that victims of wildfires and other natural disasters are exempt from state gross income tax for any amount received in settlement to replace property damaged or destroyed by those disasters."

Opponents

None on file.

LEGISLATIVE CONTACT

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