Date of Hearing: January 10, 2022

ASSEMBLY COMMITTEE ON REVENUE AND TAXATION
Autumn R. Burke, Chairwoman

AB 1249 (Gallagher) – As Amended January 3, 2022

2/3 vote. Fiscal committee.

SUBJECT: Income taxes: gross income exclusions: wildfires

SUMMARY: Allows, under the Personal Income Tax (PIT) Law and the Corporation Tax (CT) Law, a gross income exclusion to "qualified taxpayers" for amounts disbursed from the Fire Victims Trust (Trust). Specifically, **this bill**:

1) Authorizes a gross income exclusion, under the PIT Law and CT Law, for any "qualified amount" received by a "qualified taxpayer."

2) Defines "qualified amount" as any amounts received in settlement by a "qualified taxpayer" from the Trust, established pursuant to 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.

3) Defines a "qualified taxpayer" as any of the following:

   a) Any taxpayer that currently owns or previously owned real property located in, or any taxpayer that currently resides or previously resided within, the County of Amador or Calaveras, who received amounts, incurred expenses, or received amounts from a settlement arising out of or pursuant to the 2015 Butte Fire.

   b) Any taxpayer that currently owns or previously owned real property located in, or any taxpayer that currently resides or previously resided within, the County of Napa, Sonoma, Lake, Butte, Mendocino, or Solano who received amounts, incurred expenses, or received amounts from a settlement arising out of or pursuant to one or more of the 2017 North Bay Fires.

   c) Any taxpayer that currently owns or previously owned real property located in, or any taxpayer that currently resides or previously resided within, the County of Butte who received amounts, incurred expenses, or received amounts from a settlement arising out of or pursuant to the 2018 Camp Fire.

4) Requires the Trust, upon request by the Franchise Tax Board (FTB), to provide an annual list of names, addresses, payment dates, and amounts paid to "qualified taxpayers."

5) Provides that this exclusion shall apply to taxable years beginning before, on, or after the bill's effective date.

6) Allows, in prior tax years, a refund of overpayments resulting from this bill's exclusion to be made from the Tax Relief and Refund Account, as specified.

7) Provides that the provisions of this bill shall remain in effect until January 1, 2028 and are repealed as of that date.

8) Takes effect immediately as an urgency measure necessary for the immediate preservation of the public peace, health, or safety, within the meaning of Article IV of the California Constitution.

9) Makes findings and declarations.

EXISTING LAW provides that gross income shall include all income from whatever source derived, except for certain types of income that are excluded from gross income. Generally, excludes from gross income amounts of damages, other than punitive damages, received in a settlement on account of personal physical injuries or physical sickness.

FISCAL EFFECT: The FTB, in its analysis of a previous, but substantially similar, version of this bill, notes a General Fund loss of $140 million in the 2021-22 fiscal year (FY), $42 million in the 2022-23 FY, and $33 million in the 2023-24 FY.

COMMENTS:

1) The author has provided the following statement in support of this bill:

   > AB 1249 is a straightforward fix that would clarify state tax exemption criteria for victims of three of the most destructive [fires] in California's history. Victims have been through enough and deserve to receive the maximum amount of compensation from PG&E for the amount of pain and suffering the company has caused.

2) Supporters state that, "[The] Trust was created to compensate victims of several recent devastating wildfires. 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. AB 1249 would clarify that victims of three of the most destructive fires in California's history are exempt from state gross income tax for amounts received from the Trust."

3) Committee Staff Comments:

   a) *California wildfires*: California has seen a sharp increase in the severity and frequency of wildfires in the last two decades. According to the California Department of Forestry and Fire Protection (Cal Fire), 15 of the 20 most destructive wildfires in California's history have occurred in the last decade. Included on this list are the Camp Fire, the Butte Fire, and the Tubbs and Nuns fires, which are the two most destructive fires in the wider conflagration referred to as the North Bay Fires.

   b) *Pacific Gas and Electric (PG&E) bankruptcy*: In November 2018, PG&E was sued by multiple victims of the Camp Fire. In January 2019, PG&E declared bankruptcy resulting from investigative findings that the company's equipment sparked a number of wildfires, including the Camp Fire. On June 20, 2020, the United States Bankruptcy Court for the Northern District of California approved PG&E's bankruptcy plan, which established the Trust and authorized $13.5 billion in compensation to victims of the 2015 Butte Fire, the 2017 North Bay Fires, and the 2018 Camp Fire. This bill would allow taxpayers who have received compensation from the Trust to exclude those amounts from their gross income.

c) *Treatment of settlement awards*: Generally, federal and state law allows for the exclusion from gross income of amounts received in a settlement, other than punitive damages, which result from personal physical injuries or physical sickness. However, amounts resulting from emotional distress are included when calculating gross income, unless the emotional distress is the result of physical injury or sickness. Additionally, federal and state law require inclusion of attorney's fees resulting from a settlement in the calculation of gross income. Therefore, some portions of the disbursements issued from the Trust may be included in gross income. This bill would exclude all amounts disbursed from the Trust when calculating a taxpayer's gross income.

d) *What is a "tax expenditure"*? Existing law provides various credits, deductions, exclusions, and exemptions for particular taxpayer groups. In the late 1960s, United States Treasury officials began arguing that these features of the tax law should be referred to as "expenditures" since they are generally enacted to accomplish some governmental purpose and there is a determinable cost associated with each of them (in the form of forgone revenues). This bill would authorize taxpayers to exclude amounts received in settlement from the Trust.

e) *Committee's tax expenditure policy*: SB 1335 (Leno), Chapter 845, Statutes of 2014, added (Revenue and Taxation Code) R&TC Section 41, which recognized that the Legislature should apply the same level of review used for government spending programs to tax credits introduced on or after January 1, 2015. AB 263 (Burke), Chapter 743, Statutes of 2019, extended the requirements in R&TC Section 41 to all tax expenditure measures under the PIT Law, the CT Law, and the Sales and Use Tax Law introduced on or after January 1, 2020. A tax expenditure proposal must outline specific goals, purposes, and objectives that the tax expenditure will achieve, along with detailed performance indicators for the Legislature to use when measuring whether the tax expenditure meets those stated goals, purposes, and objectives. In addition to the R&TC Section 41 requirements, this Committee's policy also requires that all tax expenditure proposals contain an appropriate sunset provision to be eligible for a vote[1]. Sunsets are required because eliminating a tax expenditure generally requires a 2/3rd vote. These requirements must be satisfied before a bill can receive a vote in this Committee. This bill contains a five-year sunset and complies with Section 41 requirements.

f) *FTB analysis*: The FTB notes that the term "qualified taxpayer" contains the phrase "who received amounts, incurred expenses, or received amounts from a settlement arising out of or pursuant to" enumerated fires. It is unclear if the author intends "received amounts" to be from a source other than "received amounts from a settlement." Additionally, this bill requires that an expense was incurred, but not paid, by the taxpayer. If either of FTB's considerations are counter to the intent, the author may wish to amend this bill.

REGISTERED SUPPORT / OPPOSITION:

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[1] An "appropriate sunset provision" shall mean five years, except in the case of a tax expenditure measure providing relief to California veterans, in which case "appropriate sunset provision" shall mean 10 years.

Support

Howard Jarvis Taxpayers Association

Opposition

None on file

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