STATE OF CALIFORNIA
Franchise Tax Board

Bill Analysis

Author: Becker | Sponsor: | Bill Number: SB 1301

Related Bills: See Legislative History | Amended: June 09, 2022

SUBJECT

Green Energy Manufacturing Tax Credit

SUMMARY

This bill would, under the Personal Income Tax Law (PITL) and the Corporation Tax Law (CTL), create a tax credit for purchases of certain tangible personal property (TPP) used in manufacturing of specified clean energy products.

RECOMMENDATION

No position.

SUMMARY OF AMENDMENTS

The June 09, 2022, amendments revised the sunset date and resolved one policy consideration by adding Revenue and Taxation Code (RTC) section 41 reporting requirements.

REASON FOR THE BILL

The reason for this bill is to provide a tax credit to manufacturers producing clean energy products.

ANALYSIS

For each taxable year beginning on or after January 1, 2023, and before January 1, 2028, this bill would allow a credit to a taxpayer for 10 percent of the amount paid or incurred during the taxable year for newly installed TPP used in the manufacturing of clean energy products.

This bill would reduce the amount of credit by amounts paid or incurred that were excluded from sales and use tax under the Sales and Use Tax Law and California Alternative Energy and Advanced Transportation Financing Authority (CAEATFA).

This bill would define "clean energy products" as a products, or components used primarily in products that are in at least one of the following categories:

- Products used to produce renewable or zero carbon energy, including solar panels, wind turbines, inverters, and related balance of system components.
- Zero-emission vehicles, including battery electric vehicles, hydrogen fuel cell electric vehicles, battery packs and fuel cells for zero-emission vehicles, electric vehicle charging equipment, hydrogen fueling equipment, and other components directly related to powering vehicles without the use of fossil fuels.
- Zero-emission appliances, including heat pumps for space and water heating, induction cooktops, and other equipment used to replace equipment powered by fossil fuels in residential and commercial buildings.
- Energy storage primarily used for storing renewable or zero carbon energy.

This bill would define "eligible manufacturing costs" as the costs of newly installed TPP used in the manufacturing of clean energy products.

This bill would define "newly installed tangible personal property" as TPP that has not previously been used in the state for the purpose of manufacturing clean energy products.

The credit may be carried forward for up to seven years, until exhausted.

Any deduction or exclusion otherwise allowed under the PITL or CTL for any amount paid or incurred by the taxpayer upon which the credit is based would be reduced by the amount of the credit allowed.

The bill would be operative only for taxable years in which resources are authorized for its purposes in the annual Budget Act or other statute.

Because this bill does not specify otherwise, this credit would not reduce regular tax below tentative minimum tax (TMT).

This credit would remain in effect until December 1, 2028, and as of that date would be repealed.

This bill would require the Franchise Tax Board to provide a report to the Legislature on or before June 30, 2024, and annually thereafter, that contains both of the following elements:

- The total amount of investment associated with the tax credits in any year for which the tax credits are operative.
- The year-over-year change in the total investment associated with the tax credits.

These reporting requirements would be treated as an exception to the disclosure prohibition of the RTC.

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, 2023, and before January 1, 2028. In addition, this bill would only be operative for taxable years for which resources are authorized in the annual Budget Act or other statute.

Federal/State Law

Federal Law

Existing federal law does not have a credit comparable to that proposed in this bill.

State Law

Previous state law allowed qualified taxpayers a Manufacturers' Investment Credit (MIC) equal to 6 percent of the amount paid or incurred after January 1, 1994, and before January 1, 2004, for qualified property that was placed in service in California.

For purposes of the MIC, a qualified taxpayer was any taxpayer engaged in manufacturing activities described in specified codes listed in the Standard Industrial Classification (SIC) Manual, 1987 edition.

Qualified property was any of the following:

1) TPP defined in Section 1245(a) of the Internal Revenue Code (IRC), used in a qualified SIC code activity, and used primarily for:
    - Manufacturing, processing, refining, fabricating, or recycling of property, research and development;
    - Maintenance, repair, measurement, or testing of otherwise qualified property; or
    - Pollution control that meets or exceeds state or local standards.
2) The value of any capitalized labor costs directly allocable to the construction or modification of the property listed in #1 above or for special purpose buildings and foundations listed in #3 below.
3) Special purpose buildings and foundations that were an integral part of specified activities.

The MIC statute was repealed by its own terms and ceased to be operative as of January 1, 2004.

Under RTC 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 effectiveness of the credit.

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.

This bill does not have administrative details necessary to implement the proposed credit and determine its impacts to the department's systems, forms, and processes as discussed below.

This bill does not define "tangible personal property." This bill should specify that tangible personal property is defined in Section 1245(a) of the IRC. The absence of definition may lead to disputes between FTB and taxpayers.

This bill uses terms and phrases that are undefined, such as "newly installed," "primarily," "products used to produce renewable or zero carbon energy, including solar panels, wind turbines, inverters, and related balance of system components," "battery electric vehicles," "hydrogen fuel cell electric vehicles," "battery packs," "fuel cells," "zero emission vehicles," "electric vehicle charging equipment," "hydrogen fueling equipment," "heat pumps for space and water heating," "induction cooktops." The absence of definitions to clarify these terms could lead to disputes between taxpayers and the department, thus complicating the administration of this credit.

Typically, credits involving areas for which the FTB does not have the 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. The certificate would identify the taxpayer's eligible manufacturing costs and the amount of the credit. It is recommended that this bill be amended to include a certifying agency.

This credit would be contingent upon an appropriation in the annual Budget Act or another statute, which creates uncertainty for taxpayers and the department and could lead to increased departmental costs. If this is not the intent, the author may want to amend the bill.

This bill requires the FTB to prepare a report on the performance of the credit allowed by this bill by June 30, 2024, and annually thereafter. If the author's intent is to be able to review a report that contains complete information for the 2022 taxable year, it is recommended that the due date of the report be moved to June of 2025. For corporations filing on a fiscal year basis, with extension, a return could be filed by

September 15, 2024. The department generally needs about six months to complete return processing and compile the data needed to prepare a report. As a result, it is recommended that the due date for the report be no earlier than June of 2025, and annually thereafter while the credit is in effect. If the due date of the report remains unchanged, the report will include the information available as of the date when the report is prepared.

Additionally, this bill would require the FTB report contain the total amount of investment associated with the tax credits in any year and the year-over-year change in the total investment associated with the tax credits. However, the term "investments" is undefined in the bill. For clarity, it is recommended that the term "investments" in the reporting requirements in Section 3(b)(1)(A) and (B), be replaced with "amounts paid or incurred for eligible manufacturing costs" to match terms within the language of the bill, as follows:

- The total amount paid or incurred for eligible manufacturing costs associated with the tax credits generated by taxable year.
- The year-over-year change in the total amounts paid or incurred for eligible manufacturing costs associated with the tax credits generated for the current taxable year as compared to amounts paid or incurred for eligible manufacturing costs associated with the tax credits generated and reported for the prior taxable year.

Technical Considerations

None noted.

Policy Considerations

The credit would be allowed for eligible manufacturing costs paid or incurred either inside or outside California. Equipment that is purchased and used out-of-state and subsequently moved to this state could be eligible for the credit. If this is contrary to the author's intent, the bill should be amended.

This bill does not to limit the amount of the credit that may be taken. Tax benefits that could potentially be quite costly are sometimes limited either on a per-project or per-taxpayer basis.

This bill does not specify the taxable year in which the TPP must be purchased, which may be earlier than the taxable year in which the equipment is "installed" in this state or "placed in service" (i.e., used). Most credits involving the acquisition of an item of property provide that the credit be claimed in the same taxable year that the "placed in service date" occurs. For example, a taxpayer could within the same taxable year purchase the equipment, claim the credit, and remove the equipment from this state, or sell the equipment to a third party. The author may wish to amend the language by requiring the taxpayer to use the TPP for a specific length of time in this state, specify that the equipment must be placed in service in the taxable year.

LEGISLATIVE HISTORY

AB 904 (Grayson, 2021/2022) would have created a tax credit for purchases of certain property by certain manufacturing businesses. AB 904 did not pass out of the Assembly Revenue and Taxation Committee.

SB 676 (Alquist, Chapter 751, Statutes of 1994) made clarifying changes to the MIC and added provisions allowing the credit for leased property, but only to the lessee.

SB 671 (Alquist, Chapter 881, Statutes of 1993) enacted the MIC.

SB 445 (Ashburn, 2009/2010), AB 1998 (Dutton, 2003/2004), AB 2070 (Houston, 2003/2004), AB 2076 (Dutton, 2003/2004), and SB 1295 (Morrow, 2003/2004), each, among other things, would have reinstated the MIC. None of these bills passed out of the committee process.

PROGRAM BACKGROUND

None noted.

FISCAL IMPACT

The department anticipates minimal costs to implement this bill.

ECONOMIC IMPACT

Revenue Estimate

This bill would allow a credit of 10 percent of the amount paid or incurred by a taxpayer for eligible manufacturing costs of clean energy products. Because it is difficult to predict the frequency and amount of eligible manufacturing costs incurred by taxpayers, we cannot provide an annual estimate. However, it is assumed that for every $10 million in credits generated, approximately $5 million would be claimed in the year generated and the remaining credit would be used over the subsequent seven years.

To arrive at the offsetting tax effect of a $10 million expense deduction that would otherwise be allowed under current law, an average tax rate of 7 percent was applied resulting in an offsetting revenue gain of $700,000. The resulting net revenue loss, for taxable year 2023, would be $4.3 million.

LEGAL IMPACT

None noted.

APPOINTMENTS

None noted.

SUPPORT/OPPOSITION

Support

According to the June 17, 2022, Assembly Revenue and Taxation Committee analysis registered support for SB 1301 includes: California Chamber of Commerce and Orange County Business Council, 350 Humboldt, 350 Sacramento, 350 Silicon Valley, California Electric Transportation Coalition, and Orange County Business Council.

Opposition

According to the June 17, 2022, Assembly Revenue and Taxation Committee analysis registered opposition for SB 1301 includes California Teachers Association.

ARGUMENTS

Proponents

The Assembly Committee on Revenue and Taxation analysis dated June 17, 2022, includes the following statement from California Electric Transportation Coalition, which notes the following:

> California has already demonstrated its commitment to the production of clean energy products as evidenced by the existing sales and use tax exclusion for advanced manufacturing, which includes some clean energy components. California has also set some of the nation's most ambitious climate goals. But despite being a leader in efforts against climate change, California does not have a manufacturing tax credit specifically for clean energy products.

Opponents

The Assembly Committee on Revenue and Taxation analysis dated June 17, 2022, includes the following statement from California Teachers Association (CTA), which notes:

> Despite having the 5th largest economy in the nation, California continues to rank near the bottom of the states in the nation in per-pupil funding. According to the Education Law Center's *Making the Grade* report, California was ranked 30th in per-pupil expenditures, adjusted for regional cost differences for the 2019 fiscal year (the most recent data available). CTA believes that Prop. 98 should be protected from reductions through the creation of new or expanding existing tax expenditures.

LEGISLATIVE CONTACT

FTBLegislativeServices@ftb.ca.gov