

Date of Hearing: March 25, 2019

ASSEMBLY COMMITTEE ON REVENUE AND TAXATION

Autumn R. Burke, Chairwoman

AB 1049 (

Grayson) – As Introduced February 21, 2019

FOR TESTIMONY ONLY

Majority vote. Tax levy. Fiscal committee.

SUBJECT: Sales and use taxes: exemption: on-call volunteer fire department: equipment

SUMMARY: Provides a complete and indefinite sales and use tax (SUT) exemption for "equipment" purchased for exclusive use by an on-call volunteer fire department. Specifically, **this bill:**

- 1) Defines "equipment" as capital equipment with a sales price of \$5,000 or more.
- 2) Provides that, notwithstanding existing law, the state shall not reimburse any local agency for any SUT revenues lost as a result of this exemption.
- 3) Takes immediate effect as a tax levy.

EXISTING LAW:

- 1) Imposes a sales tax on retailers for the privilege of selling tangible personal property (TPP), absent a specific exemption. The tax is based upon the retailer's gross receipts from TPP sales in this state.
- 2) Imposes a complimentary use tax on the storage, use, or other consumption of TPP purchased out-of-state and brought into California. The use tax is imposed on the purchaser; and unless the purchaser pays the use tax to an out-of-state retailer registered to collect California's use tax, the purchaser remains liable for the tax. The use tax is set at the same rate as the state's sales tax and must generally be remitted to the California Department of Tax and Fee Administration (CDTFA).

FISCAL EFFECT: Pending

COMMENTS:

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

On-call fire departments now are a crucial part of serving and protecting the state from the growing wildfires. Established in all parts of the state, on-call fire departments routinely send staff and equipment – regardless of whether the fire is within a department's specific community – when state and local fire departments are unable to

meet the needs of their communities. Existing law does not make allowances for the fact that these on-call fire departments are at best severely underfunded to purchase or repair fire equipment.

AB 1049 would establish a sales tax exemption for equipment purchased by an on-call fire department. At an 8% sales tax rate, approximately \$2 million would go toward funding these on-call fire departments. AB 1049 will ensure that on-call fire fighters have the equipment they need to protect all Californians against increasing statewide wildfires. In short, supporting AB 1049 means promoting public safety and preparing for our future.

2) This bill is sponsored by the Contra Costa County Board of Supervisors, which notes:

Volunteer on-call fire departments provide the same service as full-time departments in areas that simply do not generate the tax revenue needed for 24 hour shift crews. For departments, such as the Crockett-Carquinez Fire Department, the cost to replace an aging fire engine can represent between 80 and 110 percent of their total yearly budget. As a result, small districts like Crockett must continue to keep older engines in service well past their recommended replacement timeframe in order to amass sufficient funds to purchase a replacement. This results in higher maintenance costs, more down time, and most importantly greater risk for our firefighters who are already making great sacrifice to serve our communities and state.

The benefits of facilitating the purchase of replacement engines are not limited to just the community surrounding the district. These smaller departments respond to calls from surrounding cities and throughout the state to help with the ever increasing large scale fires that ravage California.

3) Committee Staff Comments:

- a) *What is a "tax expenditure"?* Existing law provides various credits, deductions, exclusions, and exemptions for particular taxpayer groups. In the late 1960s, U.S. 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 (in the form of foregone revenues).

As the Department of Finance notes in its annual Tax Expenditure Report, there are several key differences between tax expenditures and direct expenditures. First, tax expenditures are reviewed less frequently than direct expenditures. Second, there is generally no control over the amount of revenue losses associated with any given tax expenditure. Finally, it should also be noted that, once enacted, it takes a two-thirds vote to rescind an existing tax expenditure absent a sunset date. This effectively results in a "one-way ratchet" whereby tax expenditures can be conferred by majority vote, but cannot be rescinded, irrespective of their efficacy or cost, without a supermajority vote.

- b) *An overview of the SUT Law:* The SUT represents the state's second largest source of General Fund (GF) revenues. Nevertheless, the past 70 years have seen a dramatic reduction in the state's reliance on the SUT and a corresponding increase in its reliance on personal income tax revenues. In FY 2019-20, SUT revenues are estimated to comprise only 19% of the state's GF revenues, down from nearly 60% in FY 1950-51.

- c) *What accounts for the state's reduced reliance on SUT revenues?* The SUT Law was enacted in a very different era. In the 1930s, California's economy was largely dominated by manufacturing, and residents mostly bought and sold tangible goods. Thus, in establishing the base for a new consumption tax, it made sense to impose the tax on sales of TPP, defined as personal property that may be "seen, weighed, measured, felt, or touched." Over the past 80 years, however, California's economy has seen dramatic growth in the service and information sectors, resulting in a significant erosion of the SUT base. For example, the Commission on the 21st Century Economy noted that spending on taxable goods represented 34.6% of personal income in 2008, down from 55.4% in 1980. As a result, tax experts and economists from across the political spectrum argue that California should expand its SUT base.

It could be argued that, while well-intentioned, additional SUT exemptions further erode an already shrinking SUT base. This, in turn, increases fiscal pressures to maintain or even increase California's relatively high SUT rate. High rates arguably promote non-compliance and encourage out-of-state purchases, placing California retailers at a competitive disadvantage. High rates also risk impacting consumer decision-making, which runs counter to widely accepted principles of sound tax policy.

- d) *What would this bill do?* This bill would enact a complete and indefinite SUT exemption for equipment purchased for exclusive use by an on-call volunteer fire department. This bill defines "equipment", in turn, to mean capital equipment with a sales price of \$5,000 or more.
- e) *Finding the right definitions:*
- e.i) *On-call volunteer fire departments:* In its current form, this bill does not define the term "on-call volunteer fire department." The author, however, has expressed a desire to take amendments defining the term by reference to Revenue and Taxation Code (R&TC) Section 6018.10(b). This section, in turn, traces its origins to legislation enacted in 2015 to provide tax relief to *all volunteer* fire departments that fundraise by selling TPP. Specifically, SB 598 (Hill), Chapter 248, Statutes of 2015, provided that all volunteer fire departments shall be considered the consumer, and not the retailer, of TPP they sell provided the profits are used exclusively to further their mission. To ensure the relief was properly targeted, SB 598 defined an all-volunteer fire department as one that meets the following requirements:
- (e.i.1) No member shall be paid a regular salary, but a member may be compensated on an hourly or per incident basis;
- (e.i.2) The organization's purpose is to protect the lives, property, and environment within a designated geographical area from fires, disasters, and emergency incidents through education, prevention, training, and emergency response; and,
- (e.i.3) The organization is regularly organized for volunteer fire department purposes and qualifies as an exempt organization, either under R&TC Section 23701d or 23701f or under Internal Revenue Code Section 501(c)(3) or 501(c)(4), having official recognition and full or partial support of the government of the county, city, or district in which the volunteer fire department is located, and that has functions having an exclusive connection with the prevention and extinguishing of fires within the area of the county, city, or district extending official recognition

for the benefit of the public generally and to lessen the burdens of the entity of government that would otherwise be obligated to furnish that fire protection.

Committee staff agrees that it makes sense to incorporate by reference this detailed definition. However, for the sake of consistency, and to avoid any potential confusion, Committee staff also suggests amending this bill to use the term “all volunteer fire department” in lieu of the current term “on-call volunteer fire department.”

- e.ii) *Equipment*: This bill currently defines exempt “equipment” as capital equipment with a sales price of \$5,000 or more. This definition, however, is rather broad. In addition, it is not clear to Committee staff what this definition is intended to encompass beyond replacement fire trucks. Finally, this definition might inadvertently give rise to a certain degree of confusion. Specifically, it is unclear if the \$5,000 threshold applies to multiple equipment items with a total price of \$5,000 or more, or a single equipment item with a price of \$5,000 or more. The author may wish to take amendments further clarifying the definition of equipment.
- f) *A blunt tool*: Even if this bill is amended to provide greater definitional precision, a SUT exemption is a blunt tool for affecting social policy. While the author's office has indicated that this bill is designed to aid rural fire departments that cannot afford equipment, this bill applies to any volunteer fire department regardless of location or financial status. Thus, rather than providing a SUT exemption, it may be preferable to appropriate funds directly via a grant program to those fire departments most in need of assistance.

In addition, it could be argued that this exemption would establish a somewhat questionable precedent for other public entity exemptions. For example, what makes a volunteer fire department more worthy of a SUT exemption than a rural school district seeking to replace an aging bus, or a rural police department buying new cruisers?

- g) *Policy on tax expenditures*: SB 1335 (Leno), Chapter 845, Statutes of 2014, added 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. This Committee has recently adopted a new policy, requiring that all new tax expenditure proposals comply with the requirements of R&TC Section 41. 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. A tax expenditure bill will not be eligible for a Committee vote unless it has complied with these requirements. The author may wish to amend this bill to specify the goals being advanced by providing a SUT exemption for specified volunteer fire department equipment.

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. According to the new policy, 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 ten years. This bill, as currently drafted, does not comply with the Committee's policy on sunsets.

h) *Prior legislation:*

h.i) SB 120 (Anderson), of the 2015-16 Legislative Session, would have provided a SUT exclusion for amounts above \$300,000 in connection with any public safety first responder vehicle purchased by a local public agency. SB 120 was held on the Senate Appropriations Committee's suspense file.

h.ii) AB 1890 (Berg), of the 2007-08 Legislative Session, would have provided a SUT exemption for fire equipment with a purchase price of \$1,000 or more per vehicle or item purchased by a volunteer fire department. The proposed exemption was limited to volunteer fire departments, as defined, located in a county with a population of 100,000 or fewer individuals or providing firefighting and emergency services for 10,000 or fewer individuals. AB 1890 was heard in this Committee for testimony only and eventually reported from the Committee without further action.

h.iii) SB 1126 (McClintock), of the 2003-04 Legislative Session, would have provided a SUT exemption for specified fire equipment purchased by a local fire department. SB 1126 failed passage in the Senate Committee on Revenue and Taxation.

REGISTERED SUPPORT / OPPOSITION:**Support**

Contra Costa County Board of Supervisors (Sponsor)

Opposition

None on file

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