SENATE COMMITTEE ON GOVERNANCE AND FINANCE; ENERGY, UTILITIES AND COMMUNICATIONS; AND NATURAL RESOURCES AND WATER
INFORMATIONAL HEARING: PROPOSITION 30:

August 10, 2022

This background paper prepares the members of the Senate Governance and Finance, the Committee on Energy, Utilities, and Communications; and Natural Resources and Water for the August 10th , 2022, hearing on Proposition 30, titled "PROVIDES FUNDING FOR PROGRAMS TO REDUCE GREENHOUSE GAS EMISSIONS BY INCREASING TAX ON PERSONAL INCOME OVER $2 MILLION. "The measure is an initiative statute that:

- Increases the Personal Income Tax Rate by 1.75% on taxable income above $2 million.
- Uses funds the tax generates to fund zero emissions vehicle infrastructure and wildfire prevention.

This paper:

- Provides background regarding personal income taxes, as well as the state policies and programs regarding Zero Emissions Vehicles (ZEV) and wildfire suppression

- Summarizes the pending initiative.

Income Taxes

California's Personal Income Tax

All income earned in or sourced to California must be reported and filed on an income tax return. Residents of California must file an individual (or joint if married or registered domestic partners) return. Non-residents can either file a non-resident return, or elect to be included in a group return.

All California Personal Income Taxpayers (PIT) pay a graduated tax rate between 1 percent and 12.3 percent, depending on the taxpayer's adjusted taxable income and filing type for that year. In November 2012, voters approved Proposition 30, which added Section 36 to Article XIII of the California Constitution, which temporarily increased the top tax rates for taxable years beginning in 2012, and ending in 2019. In November, 2016, voters extended these tax rate increases through the 2030 taxable year (Proposition 55). The current 2021 tax tables are:

Filing Type : Single or Married Filing Separately		
Income Over	*But not over*	*Calculation of tax*
$0	$9,325	1%
$9,325	$22,107	2%
$22,107	$34,892	4%
$34,892	$48,435	6%
$48,435	$61,214	8%
$61,214	$312,686	9.3%
$312,686	$375,221	10.3%
$375,221	$625,369	11.3%
$625,369	And over	12.3%

Filing Type : Married/RDP Filing Jointly or Qualifying Widow		
Income Over	*But not over*	*Calculation of tax*
$0	$18,650	1%
$18,650	$44,214	2 %
$44,214	$69,784	4%
$69,784	$96,870	6%
$96,870	$122,428	8 %
$122,428	$625,372	$9.3%
$625,372	$750,442	$10.3%
$750,442	$1,250,738	11.3%
$1,250,738	And over	12.3%

Filing Type : Head of Household		
Income Over	*But not over*	*Calculation of tax*
$0	$18,663	1%
$18,663	$44,217	2%
$44,217	$56,999	4%
$56,999	$70,542	6%
$70,542	$88,324	8%
$88,324	$425,251	9.3%
$425,251	$510,303	10.3%
$510,303	$850,503	11.3%
$850,503	And over	12.3%

In the 2021-22 fiscal year, the state collected nearly $100 billion. According to data available from the Franchise Tax Board, personal income tax collection from the top 1 percent of taxpayers accounts for almost 50 percent of total personal income tax collection. Most of the revenue collected is deposited into the State's General fund and is used to pay for state expenses such as education, corrections, health care, and other public services.

Mental Health Services Tax

In November of 2004, voters approved Proposition 63 (2004) known as the "Mental Health Services Act," which imposes an additional one percent tax on taxpayers with taxable income of $1 million or more. Funds from this tax are used to better serve individuals and their families who are at risk of serious mental health issues. Specifically, the measure focuses on prevention, early intervention, and service needs and the necessary infrastructure, technology, and training elements that effectively support the public behavioral health system. The program is currently overseen by the Mental Health Services Oversight and Accountability Commission and the Department of Health Care Services. According to the data from the Franchise Tax Board, collection of this tax totals about $2 billion each year and is included on 80,000 to 90,000 tax returns annually.

State and Local Tax Deduction

Federal law generally allows individuals to deduct their state and local income taxes, sales and property taxes (SALT) on their federal income tax return. Beginning in 2018, the Federal Tax Cuts and Jobs Act (TCJA), changed several itemized deductions, including limiting the total deduction for SALT to $10,000 ($5,000 if married filing separate) for personal income taxpayers. The SALT limitation placed on individuals is set to expire after the 2025 taxable year. The SALT cap only affects individuals, not business entities. Under TCJA, most taxpayers cannot deduct additional tax imposed by Proposition 30 for federal purposes because their state taxes exceed the $10,000 limitation.

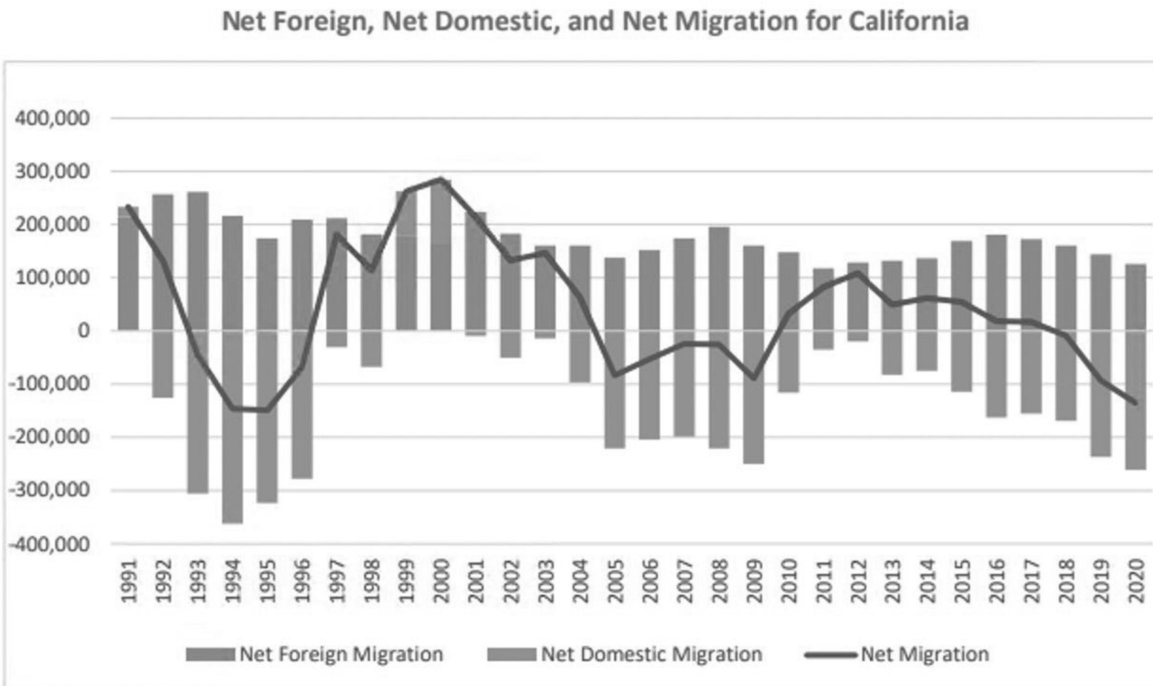
Migration and Mobility

California's personal income tax rates are already the highest in the nation. With the introduction of teleworking into more professional settings, it's easier than ever for people to move to other states.

The Franchise Tax Board notes in their 2021 report titled, *The Impact of Migration on California Income Tax Revenues*, "As shown in Figure 1, California has, in recent decades, had net domestic out-migration and net international in-migration for individuals. The balance between these two flows has shifted back and forth over time. From 2010 through 2017, the net inflow from abroad was greater than the net outflow to other states. In 2018 there was a reversal with net domestic outflow being greater than net international inflow in the years 2018-2020[1]."

[1] https://www.sco.ca.gov/Files-EO/Spotlight/Taxes_and_Migration.pdf

Figure 1:



Source: CA Department of Finance, Demographic Research Unit

The National Bureau of Economic Research, analyzed data provided by the Franchise Tax Board, in their paper titled "Behavioral Response to State Income Taxation of High Earners: Evidence from California." The researchers found that an additional 0.8% of high earning Personal Income Taxpayers left California 2013. The researchers attributed this impact to the 2012 Proposition 30 PIT tax rate increases[2]."

A March 2022 study completed by Joshua Rauh at the Stanford Graduate School of Business; Hoover Institution; and National Bureau of Economic Research notes that, "Based on our analysis, we find that the departure rates of high-income taxpayers appear highly responsive to tax policy changes like Proposition 30 and the TCJA, while out migration for low- and middle-income earners has been gradually increasing over time with in-migration not keeping pace for most income tax brackets. Similarly, the amount of income tax liability of high income out-movers prior to their move has consistently not been replaced in full by that of in-movers at the same income level, meaning the state loses revenue due to out-migration from this bracket.[3]"

ZEV

California's Climate Goals

[2] [2] https://www.nber.org/papers/w26349

[3] https://www.sco.ca.gov/Files-EO/Spotlight/Taxes_and_Migration.pdfy Joshua D. Rauh :: SSRN

The Legislature has set a number of goals to reduce GHG emissions and address climate change. The Global Warming Solutions Act of 2006 (AB 32 (Nuñez), 2006) and subsequent companion legislation SB 32 (Pavley, 2016), requires California to reduce statewide GHG emissions to 40% below the 1990 level by 2030. The 1990 level is an aggregated statewide limit, and is not sector- or facility-specific. The California Air Resources Board (CARB) is responsible for developing a Scoping Plan to detail how the state will achieve its GHG emissions reduction targets mandated by law. Governor Executive Orders (EO) also call for GHG emissions of 80% below 1990 levels by 2050, and longer-term targets for economy-wide carbon neutrality by 2045.

Transportation's impact on climate

The transportation sector generates nearly 40% of California's GHG emissions, including both the light-duty (passenger) and medium-and heavy-duty fleets. Heavy-duty diesel trucks also contribute to unhealthy levels of ozone, inhalable particulate matter, carbon monoxide, nitrogen oxides, and sulfur dioxide, affecting local air quality. Transportation sources account for roughly 80% of smog-forming emissions and 90% of diesel particulate emissions in California.

Within the transportation sector, measures to reduce GHG emissions include requiring the use of low carbon fuels, cleaner vehicles, and strategies to promote sustainable communities and improved transportation choices that reduce growth in the number of vehicle miles traveled.

ZEV goals

To further these efforts, at the end of 2020, Governor Newsom issued Executive Order (EO) N-79-20 which requires 100% of medium-and heavy-duty vehicles in the state be zero-emission by 2045 for all operations where feasible and by 2035 for drayage trucks[4]. EO N-79-20 charges CARB with developing and proposing medium-and heavy-duty vehicle regulations requiring increasing volumes of new zero-emission trucks and buses sold and operated in the state towards that goal. According to the California Energy Commission[5], ZEV car sales accounted for 16.45% of car sales in the first two quarters of 2022.

SB 1275 (de Leon, 2014) requires CARB to assess when a self-sustaining ZEV market is expected and how existing incentives may be modified to recognize expected changes in future market conditions. CARB expects once the California new ZEV market share reaches 16-20%, the market has reached the early majority segment, and there will be enough demand to help market mechanisms take over and drive the market.[6] Therefore, it is possible that in the next couple of years, state-funded incentive programs will no longer be necessary, or should be significantly modified at that time to target very specific circumstances.

ZEV charging infrastructure goals, gaps, and funding

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[4] A truck that transports shipping containers short distances

[5] https://www.energy.ca.gov/data-reports/energy-almanac/zero-emission-vehicle-and-infrastructure-statistics/new-zev-sales

[6] Fiscal Year 2020-21 Funding Plan on Clean Transportation Incentives – Appendix C: Light duty ZEV Market Update

Meeting California's ZEV goals will require a significant increase in the number of light-, medium-, and heavy-duty ZEVs on the road and a drastic increase in the infrastructure necessary to support these vehicles.

AB 2127 (Ting, 2018) codified the goal of putting at least 5 million ZEVs on California roads by 2030 and reducing GHG emission 40 percent below 1990 levels by 2030. The bill also required the California Energy Commission (CEC) to assess, every two years, the need for EV infrastructure needed to support the state's ZEV deployment goals.

According to the CEC's biennial assessment of EV infrastructure needs, California has installed more than 70,000 public and shared chargers, including over 6,000 DCFCs, and 44 hydrogen stations as of January 4, 2021. This EV Charging Infrastructure Assessment states that an additional 123,000 chargers are planned, of which about 3,600 are fast chargers, leaving a gap of about 57,000, including 430 DCFCs, to meet the 2025 infrastructure goals.[7]

For passenger vehicle charging in 2030, the EV Charging Infrastructure Assessment projects over 700,000 public and shared private chargers are needed to support 5 million ZEVs, and nearly 1.2 million chargers are needed to support about 8 million ZEVs anticipated under EO N-79-20. An additional 157,000 chargers are needed to support 180,000 medium-and heavy-duty vehicles anticipated for 2030.

Typically, the Clean Transportation Program (CTP), the main taxpayer-funded source for ZEV infrastructure, receives $100 million per year through revenue from smog abatement fees, which are scheduled to sunset on January 1, 2024. Due to recent state budget surpluses, the Legislature has appropriated additional General Fund money to ZEV infrastructure. Last year's 2021-22 Budget approved $500 million for the CTP to fund charging and hydrogen refueling infrastructure for light-duty and medium-and heavy-duty ZEVs vehicles. This year's 2022-23 Proposed Governor's Budget includes $390 million General Fund investments to deploy infrastructure to support 1,000 drayage trucks and 1,600 transit buses and $500 million General Fund for ZEV infrastructure across a range of vehicle classes. In November, 2021, Congress enacted the Infrastructure Investment and Jobs Act, which created the $5 billion National Electric Vehicle Infrastructure (NEVI) Formula Program as part of the $7.5 billion in EV infrastructure funding. This funding aims to provide a network of 500,000 ultra-fast EV charging stations along the nation's travel corridors to help make cross-country electric travel accessible to all Americans. The remaining $2.5 Billion will be awarded on a competitive basis and will be announced later this year.

[7]https://www.energy.ca.gov/programs-and-topics/programs/electric-vehicle-charging-infrastructure-assessment-ab-2127

Through NEVI formula funds, California should receive $57 million in Fiscal Year 2022, pending approval of a state plan that must be submitted by August 1, 2022. The five-year NEVI formula funding for California totals $384 million.

Ratepayer-funded EV infrastructure investments

In addition to the investments from the CTP, existing law requires electrical corporations to make investments to support transportation electrification. Most utilities make transportation electrification investments in the form of rate design to encourage electric vehicle use and support grid-responsive charging and in the form of "make-ready" infrastructure, which includes electrical upgrades to support additional charging. As of October 2021, the CPUC authorized over $1.8 billion in investor-owned utility (IOU) ratepayer-funded transportation electrification investments. To the extent that increased electric vehicle deployment substantially increases demand for electricity, utilities also propose ratepayer investments for distribution upgrades and procurement of additional energy resources. While these investments may be linked to transportation electrification, utilities frequently make these distribution and procurement proposals through general rate case and integrated resources plan (IRP) proceedings. IOU EV infrastructure investments do not include POU investments in EV infrastructure, which are approved by POU governing boards.

Wildfire Suppression

Wildfire and a changing climate

Catastrophic and devastating wildfires have occurred repeatedly in the state in recent years. Already this year, through August 1, 2022, almost 150,000 acres have already burned, evacuation orders have affected thousands, hundreds of structures have been destroyed or damaged, and, tragically, at least two Californians have died due to wildfire. In 2021, preliminary data show almost 9,000 wildland fires burned almost 2.6 million acres in the state. Slightly fewer wildland fires in 2020 burned almost 4.4 million acres – a modern record.

Nine of the 20 largest and seven of the 20 most destructive wildland fires in state history occurred in 2020 and 2021. Thousands of firefighters have been deployed to fight these fires. In the last five years from wildland fire, tens of thousands of structures – almost entirely homes – have been destroyed, insured losses incurred are in the billions of dollars, prime habitat has been destroyed or damaged, and, tragically, hundreds of lives have been lost. In addition, millions of Californians have been exposed to unhealthy air quality due to the wildfires.

One of the impacts of climate change in the state is an increase in the frequency and intensity of wildfires. In forested regions, decades of fire suppression, historic logging practices and drought have produced unhealthy forests that exacerbate the risk of an extreme wildfire developing when a fire occurs. There may be a high risk of wildland fire occurring in many of the state's diverse ecosystems, not just in forested regions, and continued development in the wildland urban interface puts more communities at risk. Managing wildfire will be important to the state meeting its climate goals. In 2020, the Air Resources Board estimated that approximately 112 million metric tons of carbon dioxide were emitted from trees and other vegetation burned in that year's wildfires.

There are multiple methods available to help reduce the risk wildland fire poses to communities across the state. These include improving the health and resiliency of the state's wildlands and forests to wildland fire through vegetation and fuels management, including prescribed fire; and home and community-hardening, including the replacement of flammable roof materials, maintaining a defensible space buffer around a home, and creating fire breaks around communities; among others.

Recent state spending on wildfire

Spending on wildfires has grown substantially in the last several years. According to the Legislative Analyst's Office, the California Department of Forestry and Fire Protection's (CAL FIRE's) total funding for fire protection, resource management, and fire prevention grew from $800 million in fiscal year (FY) 2005-06 to an estimated $3.7 billion in FY 2021- 2022. Spending on resource management and fire prevention is lower annually than for base fire protection and emergency fire suppression, and has increased recently as recognition of its importance has become widespread.

The FY 2021-2022 budget provided $988 million on a one-time basis for wildfire prevention, and improving landscape health to 18 different departments, and included language continuously appropriating $200 million annually for forest health and wildfire prevention from FY 2022-23 through FY 2028-29. Programs funded included forest health, fire prevention grants and projects, remote sensing, workforce development, and defensible space inspectors, among others. Of these moneys, $529 million was provided to CAL FIRE alone, and an additional $25 million was shared between CAL FIRE and other state agencies. The Department of Conservation's Regional Forest and Fire Capacity Program, created in 2018 to support regional collaboration for forest health and wildfire resilience by providing block grants, received $60 million.

Proposition 30: "The Clean Cars and Clean Air Act"

Initiative Overview

On February 16, 2022 proponents submitted the proposed Initiative No 21-0037 entitled, "PROVIDES FUNDING FOR PROGRAMS TO REDUCE GREENHOUSE GAS (GHG) EMISSIONS BY INCREAING TAX ON PERSONAL INCOME OVER $2 MILLION" to the Attorney General's Office. The proposal adds Division 47 (commencing with 80200) to the Public Resources Code. The proposal also adds Section 17044 to Chapter 2 (commencing with Section 17041) of Part 10 of Division 2 of the Revenue and Taxation Code. On July 1, 2022, the Secretary of State certified the submission as Proposition 30.

Stated Purpose
The “Clean Cars and Clean Air Act” finds that Electric cars are too expensive for many Californians who are already dealing with the high cost of living in this state. The purpose of this initiative is to reduce emissions from two of the state’s primary sources of greenhouse gases – transportation and wildfires –through public investments in electrification of vehicles used in California and improvements in the prevention and suppression of catastrophic wildfires while improving our air quality in the process. To help California achieve these goals, this initiative will temporarily raise the personal Income tax a tax on gross income generated by individuals, for the highest income earners in California. This increase in revenue will be used to fund ZEV programs and wildfire-related activities.

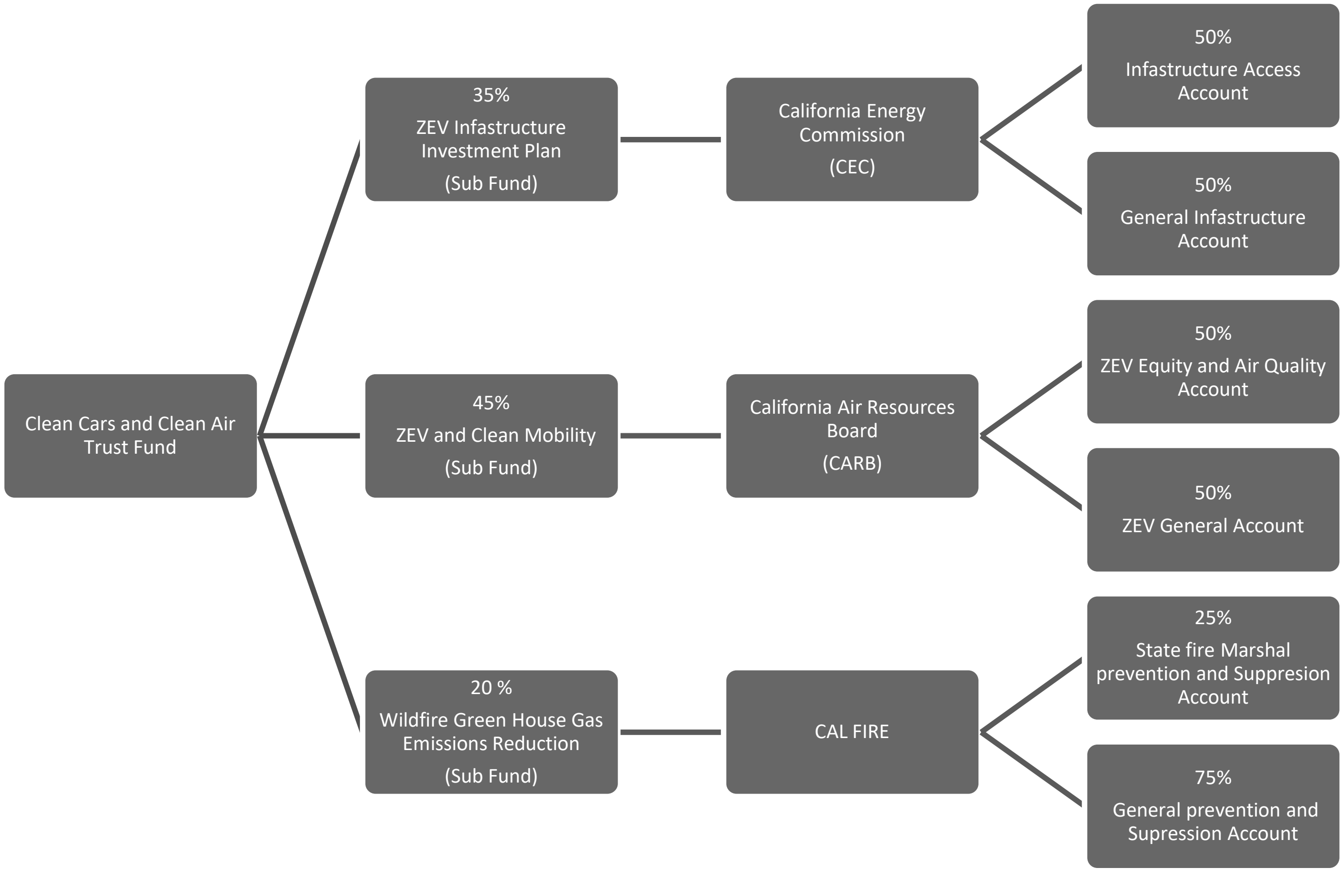
Tax Changes
This proposition imposes an additional tax on top of existing tax rates, of 1.75% on the PIT rate starting in the 2023 tax year for taxable income that exceeds $2 million. The $2 million is not adjusted for a married filing joint filers (MFJ), so the tax is more likely to be imposed on MFJ taxpayers. This additional tax will expire after the 2043 taxable year. If, for three consecutive years, the statewide greenhouse gas emissions have been reduced by 80 percent below 1990 levels, then the tax will expire in the 2030 taxable year.

According to the Legislative Analyst’s Office (LAO), this proposition is estimated to raise about $3-$4.5 billion per year in new revenue.

Fund Allocation

The additional revenue generated from the increased tax under this initiative is deposited into a new fund called the Clean Cars and Clean Air Trust Fund (CCCATF) housed in the state treasury.

After administrative costs are paid, the initiative allocates the funds received in the following ways:



The initiative continuously appropriates tax proceeds to the sub funds and caps the amount of administrative expenses at five percent for CEC, CARB and CAL FIRE. An audit must be completed by the California State Auditor every two years and by the California State Controller every four years. The initiative allows up to $600,000 per audit. The initiative authorizes amendments by the Legislature only by a three-fourths vote.

The initiative further delineates the funds a follows.

ZEV Infrastructure Investment Plan (35 percent)

The initiative requires the 35 percent of the revenue collected to CEC, with 50 percent of that funding allocated to the "Infrastructure Access Account" and the other 50 percent to the General Infrastructure Account.

CEC must allocate the money in the Infrastructure Access Account to projects, activities, and to the benefit of people in low-income and disadvantaged communities.

This sub-fund requires the following minimum spending allocations for money from both the Infrastructure Access Account and the General Infrastructure Account for five fiscal years beginning on July 1, 2023.

- 20 percent for multifamily dwelling ZEV charging stations;
- 10 percent for single-family dwelling SEV charging stations;
- 10 percent for passenger ZEV fast-fueling infrastructure; and,
- 10 percent for medium and heavy duty SEV fueling infrastructure.

ZEV and Clean Mobility (45 percent)

Requires that 45 percent of the revenue collected under this initiative be allocated to CARB. This sub-fund is then allocated 50 percent to "ZEV and Air Quality Account" and 50 percent is allocate to the "ZEV general account.[8]" CARB must allocate to promote the purchase and use of ZEV's.

CARB is charged with establishing a Factory new ZEV Incentive Program (using funds from the ZEV general account). This program is used to fund rebates, subsidies, grants, and other financial incentives for ZEVs. Applications for these programs must be prioritized as follows:

- Applications from individual California residents;
- Applications from legal entities that have employees or own property in California and individual residents, for ZEVs for high-utilization purposes;
    - High-utilization means more than 25,000 miles per year
- Applications from legal entities and state and local government agencies.

The funds collected and allocated to the ZEV and Air Quality Account must be allocated to programs that primarily benefit people who live in low-income and disadvantaged communities, as defined, for five years beginning on July 1, 2023. The initiative states that at least 2/3 of the ZEV and Clean Mobility sub-funds must be allocated to projects, programs, purposes, and activities that support the deployment of passenger ZEVs operations in the state.

Wildfire GHG Emissions Reduction (20 percent)

The measure requires that 20 percent of the revenue collected be allocated to CAL FIRE. This sub-fund is then allocated 75 percent into the General Prevention and Suppression Account and 25 percent into the State Fire Marshal Prevention and Suppression Account.

The initiative requires the primary priority for money in the General Prevention and Suppression Account be given to retaining, housing, training and hiring CAL FIRE permanent and seasonal firefighters necessary to prevent and suppress wildfires. For six fiscal years beginning July 1, 2024, the initiative requires 25% of these funds to be used for wildfire prevention and resilience efforts including:

- Improving defensible spaces around homes and communities;

[8] Until a maximum balance is reached and then 100% to the ZEV general account.

- Grants for home-hardening retrofits focused on low-income communities; and,
- Support activities and programs such as forest resilience programs, prescribed burning, watershed restoration and management, and vegetation management.

The funds collected and allocated to the State Fire Marshal Prevention and Suppression Account must fund fire prevention and suppression efforts selected by the Office of the State Fire Marshal in conjunction with a statewide apprenticeship committee established to improve the quality of education and training within the fire service and set professional standards for firefighters in the state.