

SUMMARY ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author: Ashburn Analyst: Darrine Distefano Bill Number: SB 1523

Related Bills: See Prior Analysis Telephone: 845-6458 Amended Date: May 3, 2004

Attorney: Patrick Kusiak Sponsor: _____

SUBJECT: Employer Hiring Credit

DEPARTMENT AMENDMENTS ACCEPTED. Amendments reflect suggestions of previous analysis of bill as introduced/amended _____.

AMENDMENTS IMPACT REVENUE. A new revenue estimate is provided.

AMENDMENTS DID NOT RESOLVE THE DEPARTMENT'S CONCERNS stated in the previous analysis of bill as amended April 12, 2004.

_____ FURTHER AMENDMENTS NECESSARY.

_____ DEPARTMENT POSITION CHANGED TO _____.

REMAINDER OF PREVIOUS ANALYSIS OF BILL AS AMENDED April 12, 2004. STILL APPLIES.

OTHER - See comments below.

SUMMARY

This bill would provide a hiring credit to employers with fewer than 19 employees.

SUMMARY OF AMENDMENTS

The May 3, 2004, amendments made the following changes:

- Delete the credit percentages available to the employer for the first five years of the qualified employee's employment.
- Allow a credit in an amount equal to the total number of hours worked by a qualified new employee for each year of employment multiplied by \$3.
- Redefine a "qualified new employee" as an individual who is paid qualified wages, instead of a rate of compensation of no less than \$10 per hour.
- Replace the term "person" with "individual."
- Redefine "qualified wages" to mean an amount of wages paid or incurred during the taxable year by the qualified employer to the qualified new employee that is no less than either of the following:
 - \$10 per hour, or
 - \$8 per hour plus at least 70% of the costs of the qualified new employee's health care benefits.

Board Position:

_____ S _____ NA _____ NP
_____ SA _____ O _____ NAR
_____ N _____ OUA PENDING

Legislative Director

Date

Brian Putler

5/14/04

The May 3rd amendments resolve the department's technical considerations from the April 12, 2004, analysis, however, it does not resolve the department's implementation consideration. For convenience, the implementation consideration is repeated below. Also, a revised revenue estimate, new technical, and new policy concerns are provided below. The remainder of the department's analysis of the bill from April 12th still applies.

POSITION

Pending.

ANALYSIS

IMPLEMENTATION CONSIDERATIONS

Under "qualified new employee" the bill states that the "service" must be directly related to the trade or business in a qualified area. It is not clear if this requirement means that employment must be within the qualified area or only related to the trade or business within the area. The language of the bill appears to allow the qualified new employee to work outside of the qualified area even if his or her services are related to the employer's trade or business. The author may wish to clarify that the qualified new employee must provide services within the qualified area.

Implementing this bill would require some changes to existing tax forms and instructions and information systems, which could be accomplished during the normal annual update.

TECHNICAL CONSIDERATIONS

For the definition of a "qualified new employee", the term "a person" needs to be replaced with "an individual."

Also, the bill uses and defines the term "qualified new employee." However, there are several areas in the bill where only the term "qualified employee" is used. The author may wish to add the term "new" to correctly identify the qualified employee.

ECONOMIC IMPACT

Revenue Estimate

It is estimated that revenue losses for the initial three fiscal years impacted by this bill are as follows:

Small Business Targeted Employment Hiring Credit Proposal SB 1523 as amended May 3, 2004 (<i>\$ Rounded to Nearest Million</i>)			
Fiscal Year	2005/2006	2006/2007	2007/2008
Net Revenue Loss	-2	-10	-18

Revenue Discussion

The April 12, 2004, amendments resulted in larger revenue losses over the initial three years based on a higher response rate in the first full impact year. Due to the more advantageous tax benefits of the April 12th amendments, roughly 2,100 eligible employees could be hired within a year following enactment. Under the May 3rd amendments, the projected number of employees hired in the first full year (2006) of enactment is reduced to 1,600. This decrease in eligible new jobs is due to the reduced credit over the initial years of employment and a reduced incentive in promoting new hiring.

It is projected that eligible tax credits claimed over the first full 12-month (2006) hiring period would total \$10 million based on maximum \$6,000 (\$3 per hour X 2,000 hours) credit for roughly 1,600 (\$6,000 X 1,600 ~ \$10 million) qualified new hires. For the initial operative tax year (2005), it is projected that the eligible new jobs will be small because of the specified six-month (July – December 2005) window of opportunity (300 employees X \$6,000 ~ \$2 million). In 2007, it is estimated that a total of 3,000 employees would be hired (3,000 X \$6,000 = \$18 million). This bill is estimated to have a cumulative potential impact of creating 5,100 new jobs. This change produces a revised three-year projected revenue impact of \$30 million in losses.

The estimate methodology for the May 3rd amendment reflects the revised credit computation and an augmentation in certain negative taxpayer behavior likely to occur. The April 12th amendments would have allowed an employer to claim a 50% credit in any year so long as the employer maintained a net growth in employment equal to one full-time position (as defined). With the tiered credit percentages, an employer could generate significant tax benefits if he/she had a reasonable basis to terminate a newly hired “targeted employee” after their initial year of employment. By replacing the terminated employee with *another* targeted employee, the employer could regain eligibility for a hiring credit at 50% of qualified wages, potentially producing a much larger hiring credit.

LEGISLATIVE STAFF CONTACT

Darrine Distefano
Franchise Tax Board
845-6458

darrine.distefano2@ftb.ca.gov

Brian Putler
Franchise Tax Board
845-6333

brian.putler@ftb.ca.gov