

Franchise Tax Board

**ANALYSIS OF ORIGINAL BILL**

Author: Tran Analyst: Angela Raygoza Bill Number: AB 2617  
Related Bills: See Legislative History Telephone: 845-7814 Introduced Date: February 19, 2010  
Attorney: Patrick Kusiak Sponsor: \_\_\_\_\_

**SUBJECT:** Employer Hiring Credit

**SUMMARY**

This bill would provide a tax credit for wages paid or incurred by a taxpayer first commencing to do business on or after 2010, as specified.

**PURPOSE OF THE BILL**

According to the author’s office, this bill is to provide a tax incentive to businesses to stimulate the economy and promote hiring in California.

**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, 2010.

**POSITION**

Pending.

**ANALYSIS**

FEDERAL/STATE LAW

Existing state and federal laws provide various tax credits designed to provide tax relief for taxpayers who incur certain expenses (e.g., child adoption) or to influence behavior, including business practices and decisions (e.g., research credits or economic development area hiring credits). These credits generally are designed to provide incentives for taxpayers to perform various actions or activities that they may not otherwise undertake.

Current law allows a credit for taxable years beginning on or after January 1, 2009, for a qualified employer in the amount of \$3,000 for each qualified full-time employee hired in the taxable year, determined on an annual full-time equivalent basis. The credit is allocated by the Franchise Tax Board (FTB) and has a maximum cap of \$400 million for all taxable years.

Board Position:	Department Director	Date
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The credit remains in effect until December 1 of the calendar year after the year in which the cumulative credit limit has been reached and is repealed as of that date. Any credits not used in the taxable year may be carried forward up to eight years.

### THIS BILL

Beginning on or after January 1, 2010, this bill would provide an income tax credit under the personal income tax law and corporate income tax law in the amount of 15 percent of the wages paid or incurred by a qualified taxpayer first commencing to do business on or after 2010.

This bill would define the following:

- “Qualified full-time employee” means:
  - A qualified employee who was paid qualified wages by the taxpayer for services of not less than an average of 35 hours per week.
  - A qualified employee who was a salaried employee and was paid compensation for full-time employment, within the meaning of the Labor Code, by the taxpayer.
- “Annual full-time equivalent” means either of the following:
  - In the case of a full-time employee paid hourly qualified wages, the total number of hours worked for the taxpayer by the employee (not to exceed 2,000 hours per employee) divided by 2,000.
  - In the case of a salaried full-time employee, the total number of weeks worked for the taxpayer by the employee divided by 52.
- “Qualified wages” means wages subject to Division 6 (commencing with Section 13000) of the Unemployment Insurance Code.

This bill would specify that any deduction allowed for the same qualified wages for which this bill would allow a credit, shall not be reduced by the amount of the credit.

This bill would require that all employees of the trades or businesses that are treated as related under the Internal Revenue Code would be treated as employed by a single taxpayer.

This bill would allow the credit to be carried over to future years until exhausted.

### IMPLEMENTATION CONSIDERATIONS

The department has identified the following implementation concerns and unless addressed the department would be unable to implement this bill. Department staff is available to work with the author’s office to resolve these and other concerns that may be identified.

This bill uses terms or phrases that are undefined, i.e. “qualified taxpayer,” “wages,” and “trades.” In addition, the bill defines certain terms such as “qualified full-time employee” and “annual full-time equivalent” but fails to use the terms in the bill language. The author may wish to clarify these terms in order to avoid disputes between taxpayers and the department. Further, lack of clarity would complicate the administration of this credit.

As written, it appears that current employees could qualify for this credit. If this is not the author’s intent, it is recommended the bill be amended to clarify that the credit would apply to qualified employees hired on or after January 1, 2010.

The bill would provide a credit for wages paid or incurred to a qualified taxpayer. Wages are not paid to a taxpayer, unless the author’s intentions are to provide a credit to employees. If this is not the author’s intent, it is recommended the bill be amended to provide a credit for wages paid or incurred to a qualified employee

This bill uses the term "first commencing doing business;" however, this term is not defined in the bill. Therefore, the term could be broadly interpreted. The following are examples of potential issues that could arise:

- If a member of a unitary business group that does business in California forms a new subsidiary in California, it is unclear whether the subsidiary would be considered a new business for purposes of this bill. Without clarity, a unitary business group may be able to exempt its business activities in California by shifting those activities into a separate corporation.
- A business that started as one form (for example, a sole proprietorship or partnership) could become reorganized as a different type of taxpayer (for example, a corporation or an S-corporation) and could qualify for this credit. In the absence of language, treating such entities as continuations of an existing business, as opposed to a new business, some taxpayers could change their entity type to be eligible for this credit.

## TECHNICAL CONSIDERATIONS

As written, the language of the bill is technically deficient. Amendments are necessary as discussed in the “Implementation Considerations.”

## **LEGISLATIVE HISTORY**

AB 340 (Knight, 2009/2010) would have provided a tax credit for a qualified employer in an amount equal to 5 percent of the wages of all qualified employees employed by the qualified employer during the taxable year. This bill failed passage out of the Assembly Revenue and Taxation Committee.

AB 1139 (Perez, 2009/2010) would have modified the definition of ex-offender for purposes of the existing Enterprise Zone (EZ) hiring credit. This bill failed passage out of the Assembly Revenue and Taxation Committee.

AB 1973 (Swanson, 2009/2010) would provide a tax credit to a taxpayer in an amount equal to 20 percent of the gross salary, not to exceed \$5,000 per employee for the first and second year of employment. This bill is currently on suspense in the Assembly Revenue and Taxation Committee.

AB 2630 (Cook, 2009/2010) would provide a tax credit under the Personal Income Tax Law (PITL) to an employer for a net-increase in full-time employees. AB 2630 is being heard in the Assembly Revenue and Taxation Committee on May 3.  
SB 508 (Dutton, 2009/2010), SBX6 11 (Dutton, 2009/2010), and SBX8 59 (Dutton, 2009/2010) are identical. These bills would have provided a tax credit for the first \$6,000 of wages paid or incurred to an individual documented by the Employee Development Department. SB 508 failed passage out of the Senate Revenue and Taxation Committee by the constitutional deadline; SBX6 11 (Dutton, 2009/2010) is located in the Senate Rules Committee; SBX8 59 failed passage out of the Senate Revenue and Taxation Committee without further action.

SB 612 (Runner, 2009/2010) would have provided a tax credit of \$500 per month for each qualified employee employed by a taxpayer. This bill failed passage out of the Senate Revenue and Taxation Committee.

ABX3 15 (Stats. 2009, Ch. 10) and SBX3 15 (Stats. 2009, Ch. 17) provides for a tax credit of \$3,000 for each net job increase.

## **OTHER STATES' INFORMATION**

The states surveyed include *Florida, Illinois, Massachusetts, Michigan, Minnesota, and New York*. These states were selected due to their similarities to California's economy, business entity types, and tax laws.

## **FISCAL IMPACT**

This bill would require a calculation for the credit that would require a new form or worksheet to be developed. As a result, this bill would impact the department's printing, processing, and storage costs for tax returns, instructions, and publications. These changes could be incorporated into the department's annual changes, and as such, the costs would be minor.

## **ECONOMIC IMPACT**

### Revenue Estimate

There is no revenue impact to this bill as currently written because a reference to "taxpayer" could mean corporation and accordingly a corporation cannot be an employee that receives wages and therefore, no credit could be generated. However, if written to provide a credit for hiring individual employees, such a proposal may generate an annual revenue loss in the range of \$2 billion.

## **POLICY CONCERNS**

A taxpayer could claim the credit proposed by this bill, a deduction for qualified wages, the EZ Hiring Credit or the Local Agency Military Base Recovery (LAMBRA) Credit, or the newly enacted Job Tax Credit (Calderon, Stats. 2009 Third Extraordinary Session, Ch. 17). The EZ hiring credit and LAMBRA apply to salaries paid to a qualified employee, while the Job Tax Credit and this bill apply to an increase in hours to achieve a full-time equivalent employee. Generally, a credit is allowed in lieu of any deduction or credit already allowable for the same item of expense in order to eliminate multiple tax benefits.

Generally, credits are capped with a percentage and a dollar amount; without the dollar limitation, the revenue loss associated with this bill could be significant. If the author would like to limit the revenue loss, it is suggested that, the credit be capped at a percentage of the costs paid or incurred or a specific dollar amount, whichever is less.

This bill lacks a sunset date. Sunset dates generally are provided to allow periodic review of the effectiveness of the credit by the Legislature.

This bill would allow for an unlimited carryover period. Consequently, the department would be required to retain the carryover on the tax forms indefinitely. Recent credits have been enacted with a carryover period limitation because experience shows credits typically are exhausted within eight years of being earned.

## **LEGISLATIVE STAFF CONTACT**

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