

ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author: Yee Analyst: Gail Hall Bill Number: SB 1391
Related Bills: See Legislative History Telephone: 845-6111 Amended Date: April 6, 2010
Attorney: Patrick Kusiak Sponsor: _____

SUBJECT: Employer Tax Credit/Reporting Information/New Credits Chaptered After January 1, 2011, Would Be Recaptured If Taxpayer Has Net Decrease In Full-Time Employees

SUMMARY

This bill would disallow certain credits that reduce tax if the taxpayer fails to achieve specified employment requirements.

SUMMARY OF AMENDMENTS

The April 6, 2010, amendments removed provisions pertaining to definitions under Personal Income Tax Laws (PITL) and added provisions relating to tax credits.

PURPOSE OF THE BILL

According to the author's staff, the purpose of this bill is to bring needed transparency and accountability to tax breaks given to taxpayers under PITL and Corporation Tax Law (CTL).

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately and operative for original returns filed after the effective date and specifically operative for credits enacted into law on or after January 1, 2011.

POSITION

Pending.

ANALYSIS

FEDERAL LAW\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 incentive for taxpayers to perform various actions or activities that they may not otherwise undertake.

Board Position:

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

Department Director

Date

Selvi Stanislaus

04/26/10

Internal Revenue Code sections 267, 318, and 707 provide rules relating to the current year deductibility of losses, expenses, and interest with respect to transactions between related taxpayers, rules for determining the constructive ownership of stock, and rules governing transactions between partners and partnerships, respectively.

THIS BILL

This bill would require a taxpayer doing business in the state under PITL or CTL to submit to the Franchise Tax Board (FTB) on a timely filed original return the following information:

- The number of full-time, part-time, and temporary employees employed by the taxpayer in the state.
- The amount of tax credits claimed by the taxpayer on the return for each tax credit.
- The number of full-time, part-time, and temporary jobs created by the tax credit.
- A list of occupations, job classifications, and expected average wages for the full-time, part-time, and temporary jobs created by the tax credit.
- A certification by the taxpayer that the information is true and correct and contains no knowing misrepresentations.
- The taxpayer's office mailing address and office telephone number.

This bill would provide that for any tax credits added into law on or after January 1, 2011, the credit would be disallowed and any credits previously allowed would be recaptured and the taxpayer would be liable for any credits on previous tax returns if the taxpayer has a net decrease in the number of full-time employees according to the information submitted to the FTB.

The net decrease in qualified full-time employees would be determined on an annual full-time equivalent basis by subtracting the total number of qualified full-time employees employed in the preceding taxable year by the taxpayer and by any trade or business acquired by the taxpayer during the current taxable year from the total number of full-time employees employed in the current taxable year by the taxpayer and by any trade or business acquired during the current taxable year.

This bill would define "annual full-time equivalent" to mean 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.

In addition, this bill would provide that all employees of the trades or businesses that are treated as related under either sections 267, 318, or 707 of the Internal Revenue Code would be treated as employed by a single taxpayer.

IMPLEMENTATION CONSIDERATIONS

The department has identified the following implementation concerns. Department staff is available to work with the author's office to resolve these and other concerns that may be identified.

- This bill would require a taxpayer to submit to the FTB specific data, but the bill lacks direction to the FTB on how the data would be utilized and reported. Clarity is necessary in order for the FTB to implement this bill.
- This bill lacks specific details on how to calculate the amount of credits reported on previous returns that would be recaptured if the taxpayer has a net decrease in the number of full-time employees. In addition, does the author intend that recaptured credits be included in tax in the current year, but with an interest charge on the recapture amount depending on which year the credit was claimed. The author should consider granting the FTB legislative authority to issue regulations to implement and administer the recapture of tax credits and clarify whether the recaptured amount would be added to current year's tax and subject to interest.
- This bill would apply to any credit under PITL and CTL added to law on or after January 1, 2011. It appears the author meant to target business credits, but this bill could disallow any nonbusiness credit added under PITL, such as an adoption credit. If the author meant for this bill to only impact business credits, amendments would be necessary.
- This bill uses terms or phrases that are undefined including "full-time employees," "part-time employees," "temporary employees," "full-time jobs," "part-time jobs," "temporary jobs." The absence of definitions to clarify these terms or phrases could lead to disputes with taxpayers and would complicate the administration of this bill.
- This bill would disallow credits claimed by a taxpayer if the taxpayer has a net decrease in the number of full-time employees "according to the information specified" to the FTB. One could interpret this sentence to mean that the FTB could not audit the data submitted annually to the FTB and determine that a credit should be disallowed or recaptured. The author should consider clarifying if the FTB may audit the information submitted to the FTB by the taxpayer.
- The bill discusses "qualified full-time employees" but it is unclear what the difference is between a "qualified full-time employee" and a "full-time employee." If there is no difference, the word "qualified" should be deleted.

TECHNICAL CONSIDERATIONS

The department has identified the following technical concerns. Department staff is available to work with the author's office to resolve these and other concerns that may be identified.

1. This bill's requirement for taxpayers to submit specific information to the FTB would be operative for original returns filed after the effective date, which would apply to returns for taxable years beginning on or after January 1, 2010, yet the bill applies to tax credits added into law on or after January 1, 2011. If the author would like these operative dates to be the same, amendments would be necessary.
2. On page 3, line 9, it appears the phrase "current taxable year" should be changed to "preceding taxable year" for consistency in calculating the total number of full-time employees.
3. In subdivision (b) of section 23603, the phrase "for any credit against the "net tax," as defined in Section 17039," refers to PITL instead of CTL. This phrase should be amended to "for any credit against the "tax," (as defined in Section 23036)."

FISCAL IMPACT

The department's costs to administer this bill cannot be determined until implementation concerns have been resolved because it is unclear to what extent the department would be required to audit, capture, and report data to the Legislature.

ECONOMIC IMPACT

This bill does not have any revenue effect because it does not alter any provisions of current tax law.

This bill would place constraints on potential future changes to tax law. The effects of this bill would be incorporated into the revenue estimates for future proposals to add tax expenditures; but cannot be estimated now because we do not know what those future proposals will be.

LEGISLATIVE STAFF CONTACT

Legislative Analyst
Gail Hall
(916) 845-6111
gail.hall@ftb.ca.gov

Revenue Manager
Monica Trefz
(916) 845-4002
monica.trefz@ftb.ca.gov

Legislative Director
Brian Putler
(916) 845-6333
brian.putler@ftb.ca.gov