

SUMMARY ANALYSIS OF AMENDED BILL

Author: Dutton Analyst: Angela Raygoza Bill Number: SB 508
 Related Bills: See Prior Analysis Telephone: 845-7814 Amended Date: May 5, 2009
 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 DEPARTMENTS CONCERNS stated in the previous analysis of bill as introduced/amended _____.

FURTHER AMENDMENTS NECESSARY.

DEPARTMENT POSITION CHANGED TO _____.

REMAINDER OF PREVIOUS ANALYSIS OF BILL AS INTRODUCED

February 26, 2009, STILL APPLIES.

OTHER – See comments below.

SUMMARY

This bill would allow a tax credit for wages paid by a qualified employer to qualified employees, as defined.

SUMMARY OF AMENDMENTS

The May 5, 2009, amendments would expand the definition of a qualified employee.

As a result of the May 5, 2009, amendments, the “This Bill” and “Economic Impact” discussions as provided in the department’s analysis of the bill as introduced February 26, 2009, have been revised.

The “Implementation Considerations,” “Technical Considerations,” and “Policy Concerns” are provided below for convenience. The remainder of the February 26, 2009, analysis still applies.

Board Position:	Asst. Legislative Director	Date
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ANALYSIS

THIS BILL

Beginning on or after January 1, 2009, this bill would provide a tax credit for a qualified taxpayer for wages paid or incurred to a qualified employee in an amount equal to the following:

- 25 percent for an employee that is employed for at least 120 hours, but less than 400 hours.
- 40 percent for an employee that is employed at least 400 hours.

The credit would be allowed for the first \$6,000 of wages paid or incurred to each qualified employee during the taxable year.

This bill would define the following:

- “Qualified employee” means an individual who is any of the following, as documented by the Employee Development Department (EDD):
 - A recipient of CalWORKs benefits,
 - A parolee,
 - A veteran, as defined in Section 980 of the Military and Veterans Code,
 - An eligible recipient of unemployment insurance benefits,
 - A recipient of unemployment insurance benefits, or
 - A person on probation.
- “Qualified taxpayer” means a taxpayer that is a person or entity engaged in a trade or business within California that has its principal office located in California

This bill would require the qualified taxpayer to comply with the following:

- Obtain a certificate from EDD certifying that a qualified employee is employed with the qualified taxpayer, and
- Retain a copy of the certificate and provide it upon request to the Franchise Tax Board (FTB).

This bill would provide rules for aggregating affiliated employers for purposes of determining the credit. This bill would require that the credit be calculated by using a trade or business' proportionate share of qualified wage expenses. In addition, for any calendar year ending after an acquisition of a major portion of a trade or business of another employer or of a separate unit, the employment relationship between a qualified employee and an employer would not be treated as terminated if the qualified employee continues to be employed in that trade or business.

This bill would reduce the expense deduction for wages paid to qualified employees by the amount of the credit.

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

IMPLEMENTATION CONSIDERATIONS

Because EDD would certify that the qualified employee meets the requirements of this bill, the department would have no implementation concerns with the bill.

TECHNICAL CONSIDERATIONS

Amendments 1 and 3 have been provided to correct technical errors.

This bill provides rules for aggregating affiliated employers for purposes of determining an employee tax credit. Because this bill lacks language to limit the number of employees and the amount of wages paid per employer, the rules for aggregating employers are unnecessary. It is recommended that the bill be amended to delete these provisions.

On page 3, line 16, and page 5, line 4, this bill specifies the credit would be reduced by subdivision (g). Subdivision (g) references unlimited credit carryovers, not reductions. It is recommended that the bill be amended to delete the reference to subdivision (g).

The bill does not limit the wages to California employees. It appears that the author intends to limit the wages paid to only California employees. Amendments 2 and 4 have been provided to accomplish this result.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue losses:

Estimated Revenue Impact of SB 508 As Amended On May 5, 2009 For Taxable Years Beginning On or After January 1, 2009 Enactment Assumed After June 30, 2009 (\$ in Billions)			
Fiscal Year	2009-10	2010-11	2011-12
Revenue Loss	-\$1.7	-\$2.1	-\$2.7

This analysis does not consider the possible changes in investment activity, employment, personal income, or gross state product that could result from this bill.

Revenue Discussion

The revenue impact of this bill would depend on the amount of wages paid to qualified employees by qualified employers and the amount of credits that would be used to offset tax liabilities in each year.

This estimate was developed in the following steps:

Step 1- Estimate the number of qualified employees for each of the five targeted classes:

Unemployed – 1.56 million

Based on data from the Bureau of Labor Statistics and the Current Population Survey, it is estimated that 30 percent of new hires had been formerly unemployed. The data revealed that approximately 45 percent of the labor force finds a new job at some point during a year. This figure is based on an annualized average using labor turnover percentages for the last six months of 2008. [(12.7 million in private employment x 45%) – 0.5 million new entrants into labor force] x 30% ≈ 1.56 million]

Veterans – 1.19 million

According to Census data, approximately 55 percent of California's 2.8 million veterans are employed. Approximately, 77 percent of employees work for the private sector, resulting in 1.19 million military veteran employees (2.8 million veteran's employed x 55% x 77% ≈ 1.19 million)

Cal-Works – 51,000

Department of Social Services data indicate approximately 51,000 Cal-Works recipients are employed.

Parolees – 37,000

Bureau of Justice Statistics data was used to derive an estimated population of approximately 120,000 parolees annually in California. It is estimated that approximately 30 percent of them will become employed in any given year. (120,000 x 30% ≈ 37,000)

Probationers – 248,000

Bureau of Justice Statistics indicate there are an estimated 644,000 persons on probation. It is assumed that 50 percent of those on probation would get a job. Of those who get a job, 77 percent would work in the private sector. (644,000 x 50% x 77% ≈ 248,000)

TOTAL – 3.09 million qualified employees

The 3.09 million total (1.56 + 1.19 + .05 + .04 + .25) would be reduced by 5 percent to account for overlap among the five subgroups resulting in an actual total of approximately \$2.9 million (3.09 million employees x 95% ≈ 2.9 million)

Step 2- For purposes of this estimate it was assumed that 90 percent of employees would qualify their employer for the \$2,400 credit for the maximum credit of 40 percent of wages. The remaining 10 percent would yield an average credit of \$1,000 for the minimum credit of 25 percent of wages. This would total approximately \$6.5 billion [(2.9 million x 90% x \$2,400) + (2.9 million x 10% x \$1,000)] in credits. The \$6.5 billion in credits would be reduced by 8 percent because employers would be unable to claim a deduction for wages included in the credit, resulting in total credits generated of approximately \$6.1 billion (\$6.5 billion x 92%).

For the 2009 taxable year, it is estimated that 80 percent or approximately \$4.9 billion ($\$6.1 \text{ billion} \times 80\%$) of the credits generated would be claimed because of sufficient tax liability. Of the \$4.9 billion claimed ($\$6.1 \text{ billion} \times 80\%$), it is assumed approximately \$3 billion ($\$4.9 \text{ billion} \times 60\%$) would be claimed on original 2009 income tax returns and approximately \$1.2 billion ($\$4.9 \text{ billion} \times 25\%$) would be accrued to fiscal year 2009-10 from amended income tax returns. The remaining \$700,000 would be claimed in subsequent years.

It is assumed that 20 percent or approximately \$840 million ($\$4.3 \text{ billion} \times 20\%$) of the accrued \$4.2 billion ($\$3 \text{ billion}$ from 2009 returns + $\$1.2 \text{ billion}$ accrued to fiscal year 2009-10) could be applied against 2009 tax liabilities. Beginning in taxable year 2010, the remaining \$3.4 billion of credits ($\$4.2 \text{ billion} - \840 million) would be carried forward and used equally over the next eight years at a rate of approximately \$430 million per year. ($\3.4 billion in credits \div 8 years to carryover \approx \$430 million)

In addition, for taxable year 2010, approximately \$1.3 billion in credits used on original and amended returns are projected for a total of approximately \$1.7 billion ($\1.3 billion generated credits in 2010 + $\$430 \text{ million}$ in carryovers) in revenue losses. Approximately one-half of the \$1.7 billion impact for tax year 2010, or approximately \$850 million ($\$1.7 \text{ billion} \times 50\%$), is assumed to be realized during the 2009-10 fiscal year from reduced estimated tax payments, for a total impact in 2009-10 of approximately \$1.7 billion ($\840 million for the 2009 taxable year + $\$850 \text{ million}$ for the 2010 taxable year).

This analysis assumes that only California employees qualify the employer for the credit, although the bill as amended does not contain this limitation. This estimate assumes that the credit would be allowed for a taxable year in which the employee was unemployed. In other words, an employer could not claim the credit for the 2011 hiring of an employee who was unemployed during the 2009 calendar year.

POLICY CONCERNS

Because this bill fails to specify otherwise, a taxpayer could potentially claim the credit proposed by this bill, the newly enacted Job Tax Credit (Calderon, Stats. 2009 Third Extraordinary Session, Ch. 17), the Enterprise Zone Hiring Credit, and the Local Agency Military Base Recovery Credit using the same employee wages. Generally, a credit is allowed in lieu of any deduction or credit already allowable for the same item of expense to eliminate multiple tax benefits.

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.

This credit would be limited to an employer whose principal office is located in California. Although the principal office could be the location of where the operation is managed, not where the work is performed, restrictions based on the location of a business could be subject to challenge as unconstitutional discrimination in favor of local commerce.

This bill would provide an incentive to an employer who pays a maximum of \$6,000 of wages to qualified employees who works less than 400 hours per year, thereby encouraging an employer to hire five qualified employees per year for a credit of \$30,000 rather than one qualified employee for 2000 hours for a credit of \$6,000. Consequently, part-time employment may increase at the expense of full-time employment.

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FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO SB 508
As Amended May 5, 2009

AMENDMENT 1

On page 2, line 22, strikeout "person" and insert:

individual

AMENDMENT 2

On page 2, after line 25 insert:

- (3) "Wages" means the amount of wages subject to Chapter 6 (commencing with 13000) of Part 6 of Division 6 of the Unemployment Insurance Code.

AMENDMENT 3

On page 4, line 10, strikeout "person" and insert:

individual

AMENDMENT 4

On page 4, after line 13, insert:

- (3) "Wages" means the amount of wages subject to Chapter 6 (commencing with 13000) of Part 6 of Division 6 of the Unemployment Insurance Code.