Franchise Tax Board

ANALYSIS OF AMENDED BILL

Author:	Hill	Analyst:	Jahna Alvarado	Bill Number:	AB 1278
Related Bills:	See Legislative History	Telephone:	845-5683	Amended Date:	May 18, 2011
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: GTEDA Hiring Credit/Limit Hiring Credit To Increase In Total Employment For Businesses Relocating Into a GTEDA

SUMMARY

This bill would, for taxpayers that relocate from a location within the state to a Geographically Targeted Economic Development Area (GTEDA), modify the calculation of the GTEDA hiring credit.

RECOMMENDATION AND SUPPORTING ARGUMENTS

No position.

Summary of Amendments

The May 18, 2011, amendments removed all of the bill's provisions, which related to an employer school volunteer credit, and replaced them with the provisions discussed in this analysis.

PURPOSE OF THE BILL

It appears the purpose of this bill is to place a limit on the GTEDA hiring credit that would be available to a taxpayer that relocates to a GTEDA from another location within the state.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately upon enactment and would apply to taxpayers that relocate from a location within the state to a location within a GTEDA during a taxable year beginning on or after January 1, 2011.

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.

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Existing federal law provides special tax incentives for empowerment zones and enterprise communities to provide economic revitalization of distressed urban and rural areas.

Under the Government Code, state law provides for several types of GTEDAs: Enterprise Zones (EZs), Manufacturing Enhancement Areas (MEAs), Targeted Tax Areas (TTAs), and Local Agency Military Base Recovery Areas (LAMBRAs).

Under the Revenue and Taxation Code (R&TC), existing state law provides special tax incentives for taxpayers conducting business activities within a GTEDA, including a hiring credit.

A business located in a GTEDA may reduce tax by a percentage of wages paid to qualified employees. A qualified employee must be hired after the area is designated as an economic development area and meet certain other criteria. At least 90 percent of the qualified employee's work must be directly related to a trade or business located in the GTEDA and at least 50 percent must be performed inside the GTEDA. The business may claim up to 50 percent of the wages paid to a qualified employee as a credit against tax imposed on income from a trade or business operating within a GTEDA.

The credit is based on the lesser of the actual hourly wage paid or 150 percent of the current state minimum hourly wage (under special circumstances for the Long Beach EZ, the maximum is 202 percent of the minimum wage). The amount of the credit must be reduced by any other federal or state jobs tax credits, and the taxpayer's deduction for ordinary and necessary trade or business expenses must be reduced by the amount of the hiring credit. Certain criteria regarding who may be a qualified employee and certain limitations differ between the various GTEDAs. Taxpayers operating in a GTEDA are allowed the hiring credit for employing "qualified employees." "Qualified employees" for GTEDAs are defined by reference to various state and federal public assistance programs. The categories of individuals considered qualified employees for the various GTEDAs are substantially similar but not identical. A taxpayer located in a GTEDA is allowed a credit of up to 50 percent of wages paid to "qualified employees" in the first year, decreasing by 10 percent each year thereafter. The taxpayer is required to obtain a voucher certificate for each of its "qualified employees." The voucher certificates are issued by the Employment Development Department (EDD) or the local (within the same GTEDA as the workplace of the employee) agency familiar with the public assistance statutes.

THIS BILL

This bill would limit the GTEDA hiring credit for employers that relocate to a GTEDA from a location within the state to the credit attributable to the number of employees that exceeds the number of employees at the employer's previous location.

The number of employees at the previous location and the type of jobs undertaken would be established by the Employment Development Department (EDD).

This bill provides for three exceptions from the limit that would be established:

1. Employees who undertake core work activities or activities that are the primary job duties of the employee that are significantly different from those activities at the previous location, as determined by the EDD;
2. Employees of taxpayers that receive a bona fide offer to relocate to another state; and
3. Employees who relocate as a result of a natural disaster, civic unrest, or eminent domain proceeding.

<u>IMPLEMENTATION CONSIDERATIONS</u>

Department staff has identified the following implementation considerations for purposes of a high level discussion; additional concerns may be identified as the bill moves through the legislative process. In order for the Franchise Tax Board (FTB) to implement this bill, clarification is necessary for the following issues.

It is unclear whether this bill would limit the existing wage-based credit for taxpayers that relocated to a GTEDA from another location within the state or would create a new, yet-to-be-defined credit for these taxpayers. Lack of clarity can lead to disputes with taxpayers and would complicate the administration of this credit.

It is unclear whether or how the limitation would apply when a taxpayer relocates from one GTEDA to another GTEDA, or relocates within the same GTEDA. If it is the author's intention that the limitation would apply only to relocations from a location within the state that is outside a GTEDA to a location that is within a GTEDA, this bill should be amended.

This bill uses terms and phrases that are undefined, i.e., "activities that are the primary job duties of the employee that are significantly different from those activities at the previous location," "bona fide offer to relocate to another state," "type of job undertaken," and "undertake core work activities." The absence of definitions to clarify these terms could lead to disputes with taxpayers and would complicate the administration of this credit.

It is unclear how the credit would be calculated under the proposed limitation because the basis for determining the limitation on the credit (number of employees in excess of a specified amount) and the basis for calculating the amount of the credit (percentage of a specified employee's wages) are inconsistent. For example, if a taxpayer exceeded employment at the previous location by 10, would the wages paid to the most recently hired 10 employees be used to calculate the credit? The 10 employees with the highest wage? For ease of administration, clarity of language, and internal harmony and consistency with the existing credit language, it is recommended that this bill be amended.

The bill is silent on whether the limitation would apply for a limited period, e.g., the taxable year that the relocation occurred in, or would apply in perpetuity. If it is the author's intention that the limitation would be applicable for a specified period, this bill should be amended.

The bill is silent on how, when, and to whom the information required to be "established by the EDD" would be reported.

It is unclear what the specified “exceptions to this subdivision” are excepted from. If it is the author’s intention that the specified exceptions would be excluded from the calculation of the credit limitation, this bill should be amended.

It is unclear what documentation, if any, would be available to a taxpayer, the FTB, or both, to document whether an employee had relocated as a result of a bona fide offer to relocate to another state, or due to the effects of a natural disaster, civic unrest, or eminent domain proceeding. Inadequate availability of documentation could lead to disputes with taxpayers and would complicate the administration of this credit.

LEGISLATIVE HISTORY

AB 103 (Assembly Budget Committee, 2011/2012) would, among other things, for taxable years beginning on or after January 1, 2011, modify eligibility for, and the calculation of, the GTEDA hiring credit for taxpayers that relocate to a GTEDA from a location within the state. AB 103 is currently pending before the Senate.

AB 231 (Perez, 2011/2012) would make a number of changes to the existing GTEDA tax credits, including revising the calculation of the amount of the hiring credit and requiring that a taxpayer complete a registration process prior to being eligible for GTEDA tax credits. AB 231 is currently pending before the Assembly Committee on Jobs, Economic Development, and the Economy.

SB 79 (Senate Budget & Fiscal Review, 2011/2012) would, among other things, for taxable years beginning on or after January 1, 2011, repeal the GTEDA tax incentive provisions of the R&TC and would eliminate the carryover of unused GTEDA credits. SB 79 is currently pending before the Assembly Committee on Budget.

SB 301 (DeSaulnier, 2011/2012) would, for applications for EZ designation that are submitted on or after January 1, 2012, limit the size of a proposed EZ when the proposed EZ’s boundaries overlap the boundaries of one or more existing or expired EZs (previously designated EZs). SB 301 is currently in the Assembly Committee on Jobs, Economic Development, and the Economy

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.

Florida allows several incentive provisions to encourage businesses in the revitalization of enterprise zones. The Florida Enterprise Zone Act and various tax incentive provisions are set to expire on December 31, 2015.

Illinois has 95 enterprise zones, *Massachusetts* has an Economic Development Incentive Program*, Michigan* has in excess of 150 geographic areas designated as Renaissance Zones, and *Minnesota* has 5 zone-based tax incentive programs, and *New York* has 72 Empire Zones.

New York's Empire Zone program sunset as of June 30, 2010. Businesses certified in the program prior to the sunset date remain in the program, and continue to be eligible for all the Empire Zone benefits, for the rest of their benefit period as long as they remain in compliance with the law and Empire Zone regulations.

FISCAL IMPACT

The department's costs to administer this bill are unable to be determined until implementation concerns have been resolved. As the bill continues to move through the legislative process and implementation concerns are resolved, costs will be identified and an appropriation will be requested, if necessary.

ECONOMIC IMPACT

The economic impact of this bill on the state's income tax revenue is unable to be determined because numerous assumptions regarding how to calculate the credit would be required to produce an estimate. The accuracy of the estimate would be based on the accuracy of the assumptions, which are incapable of being ascertained.

SUPPORT/OPPOSITION

Support: None provided.

Opposition: None provided.

ARGUMENTS

Pro: Proponents could advocate that the GTEDA hiring credits are intended to incentivize job growth and are properly limited to job growth that occurs subsequent to a business relocating within the state to a GTEDA location.

Con: Opponents could argue that the GTEDA hiring credits enhance the retention of existing businesses by providing an incentive to relocate within the state.

LEGISLATIVE STAFF CONTACT

Jahna Alvarado
Legislative Analyst, FTB
(916) 845-5683
jahna.alvarado@ftb.ca.gov

Patrice Gau-Johnson
Asst. Legislative Director, FTB
(916) 845-5521
patrice.gau-johnson@ftb.ca.gov