Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

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Related Bills:	See Legislative History	Telephone:	845-5683	Introduced Date:	February 22, 2012
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Qualified Veteran Hiring Credit

SUMMARY

This bill would establish an income tax credit for wages paid to a qualified veteran.

RECOMMENDATION

No position.

REASON FOR THE BILL

It appears that the reason for the bill is to incentivize employers to hire disabled or currently unemployed veterans to bring them back into the workforce, thus reducing the rate of unemployed veterans.

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, 2012.

ANALYSIS

Existing state and federal laws provide various tax credits designed to provide tax relief for taxpayers that incur certain expenses 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.

Existing state and federal laws allow a taxpayer to deduct expenses paid or incurred in the ordinary course of a taxpayer's trade or business, including employee wages and benefits.

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FEDERAL LAW

Under existing federal law, the Work Opportunity Tax Credit program, an employer may qualify for a tax credit of 40 percent of the qualified first-year wages, as specified, paid to an employee that is a member of a designated target group, including certain categories of qualified veterans, as specified. The maximum amount of qualified first-year wages that may be included in the credit calculation varies depending upon the individual veteran's qualifying category as shown below:

- $6,000 for an individual that is a qualified veteran because they:
  - Are a member of a family receiving Food Stamps, or
  - Have an aggregate period of unemployment equal to or exceeding 4 weeks (but less than 6 months) during the one year period ending on the hiring date.
- $14,000 for a qualified veteran that has an aggregate period of unemployment equal to or exceeding 6 months during the one-year period ending on the hiring date.

The maximum qualified first-year wages that may be included in the calculation of the credit is greater for veterans that are entitled to compensation for a service connected disability, and are currently:

- $12,000 for a qualified veteran entitled to compensation for a service connected disability that has a hiring date that is not more than one year after having been discharged or released from active duty.
- $24,000 for a qualified veteran entitled to compensation for a service connected disability that has an aggregate period of unemployment during the one year period ending on the hiring date equal to or exceeding six months.

STATE LAW

The New Jobs credit[1] enacted in 2009 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) on a first-come-first-served basis and has a maximum cap of $400 million for all taxable years. 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.

Under the Government Code, state law provides for several types of geographically targeted economic development areas (G-TEDAs): 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, existing state law provides special tax

[1] Although the New Jobs Credit is referred to as the "Small Business Hiring Credit" in the California Income Tax Expenditures report for December 2011 <https://www.ftb.ca.gov/aboutftb/Tax_Expenditure_Report_2011.pdf>, the name in common use on the department's forms, instructions, and website is used in this analysis.

incentives for taxpayers conducting business activities within a G-TEDA including a hiring credit. A business located in a G-TEDA is eligible for a hiring credit equal to a percentage of wages paid to qualified employees. A qualified employee must be hired after the area is designated as a G-TEDA 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 G-TEDA and at least 50 percent of the employee's services must be performed inside the G-TEDA.

The credit is based on the lesser of the actual hourly wage paid or 150 percent of the current 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. Any credits not used in the taxable year may be carried forward until they are exhausted.

The Corporation Tax Law (CTL) allows the assignment of certain eligible credits to taxpayers that are members of a combined reporting group. "Assignment" refers to the ability of a taxpayer that is a member of a combined reporting group to elect to transfer certain unused credits to a related corporation, as specified. The election to transfer any credit is irrevocable once made and is required to be made on the taxpayer's original return for the taxable year in which the assignment is made.

THIS BILL

For taxable years beginning on or after January 1, 2012, this bill would allow a tax credit in an amount equal to an unspecified percentage of qualified first-year wages paid by a taxpayer to a qualified veteran during the taxable year.

This bill would define the following terms:

- "Qualified veteran" would be defined as having the same meaning as Section 51(d)(3) of the Internal Revenue Code (IRC) as of the general conformity date of January 1, 2009.[2] Qualified veteran under IRC section 51(d)(3) would mean: any veteran that is certified by the designated local agency as:
    - Being a member of a family receiving assistance under a supplemental nutritional assistance program under the Food and Nutrition Act of 2008 for at least a 3 month period ending during the 12 month period ending on the hiring date, or
    - Entitled to compensation for a service-connected disability, and either
        - Having a hiring date within 1 year of their discharge or release from active duty in the Armed Forces of the United States, or
        - Having an aggregate period of unemployment of 6 months or more during the 1 year period ending on the hiring date. Or
    - Being unemployed for a total period that is either:
        - equal to or greater than 4 weeks and less than 6 months during the 1 year period that ends on the hiring date.
        - equal to or greater than 6 months during the 1 year period that ends on the hiring date.

[2] SB 401 (Stats. 2010, Ch. 14).

- "Qualified wages" would be defined as having the same meaning as Section 51(b) of the IRC as of the current general conformity date of January 1, 2009[3], as wages paid to individuals that are members of a targeted group during the 1 year period beginning with the day that the individual begins work for the employer (qualified first-year wages). The maximum amount of "qualified first-year wages" for an individual that is a qualified veteran would be $6,000, or, in the case of a veteran entitled to compensation for a service-related disability, $12,000.

The FTB would be authorized to prescribe any necessary or appropriate rules, regulations, guidelines, or procedures.

This bill would exempt from the Administrative Procedures Act, any standard, criterion, procedure, determination, rule, notice, or guideline established or issued by the FTB to implement this credit.

IMPLEMENTATION CONSIDERATIONS

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 FTB to implement this bill, clarification is necessary for the following issues.

The bill fails to specify the percent of specified wages that would be used to compute the credit. Absent this information, the FTB would be unable to administer the credit and would be unable to determine the credit's estimated impact on California revenue.

This bill adopts the federal definition of qualified veteran and qualified wages by reference. When conforming to federal law by reference, unless otherwise provided, the incorporation of federal law is as of the current conformity date, January 1, 2009. For example, because the bills fails to specify otherwise, the federal law change effective November 21, 2011, that increased the federal maximum qualified wages for certain categories of qualified veterans would be inapplicable and the lower qualified wages amount in effect as of January 1, 2009, would apply. The author may wish to specify the version of the federal law that the author intends to apply in determining the credit provided under this bill.

The credit would be allowed for qualified wages paid or incurred either inside or outside California. Recent wage-based credits have required that wages be subject to withholding under California's Unemployment Insurance Code. The author may wish to consider clarifying the definition of qualified wages that the author intends to apply in determining the credit provided under this bill.

[3] The federal maximum "qualified first-year wages" for qualified veterans was increased to (1) $12,000 for a recently discharged veteran, (2) $14,000 for a veteran that was unemployed for 6 months or more during the 1 year period preceding the hiring date, and (3) $24,000 for a veteran with a service-related disability that was unemployed for 6 months or more during the 1 year period preceding the hiring date. Vow To Hire Heroes Act Of 2011, P.L. 112-56, Sec. 261(a), November 21, 2011.

Although the definition of qualified veteran includes the requirement that an individual be certified by the designated local agency as meeting certain criteria, the bill lacks a requirement that the certification be provided to the FTB upon request. For ease of administration and consistency with other certificated credits, it is suggested that the bill be amended to require that certification as a qualified veteran be provided to the FTB upon request.

LEGISLATIVE HISTORY

SB 1056 (Denham, et. al, 2010) would have provided a tax credit in an amount equal to 25 percent of the qualified wages, not to exceed $6,000, paid to employees who are qualified veterans. SB 1056 failed passage out of the Senate Committee on Revenue and Taxation.

SB X6 7 and SB X8 63 (Denham, et. al, 2010) would have provided a tax credit in an amount equal to 25 percent of the qualified wages, not to exceed $6,000, paid to employees who are qualified veterans. SB X6 7 failed passage out of the Senate Committee on Revenue and Taxation. SB X8 63 failed to move out of the Senate Rules Committee.

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 businesses located in an EZ a credit based on wages paid to new employees. Other wage-based credits are offered to businesses that are located in high crime areas or in rural areas. These credits would be applicable, but not limited, to employees that are veterans.

Illinois allows a credit in an amount equal to 10 percent, but no greater than $1,200 of the gross wages paid by a taxpayer to a qualified veteran in the course of that veteran's sustained employment during the taxable year.

Massachusetts allows a Full Employment credit to employers who participate in the Full Employment Program and continue to employ a participant for at least one full month. The taxpayer may claim a credit of $100 per month of eligible employment per participant, up to $1,200 per participant. This credit would be applicable, but not limited, to employees that are veterans.

Michigan and *Minnesota* do not offer wage credits.

New York law provides for several wage based credits. The Excelsior jobs tax credit is a credit for each net new job created in New York State and is calculated as 6.85 percent of gross wages. The credit for employing a disabled person is equal to 35 percent of the first $6,000 in "qualified first-year wages" earned by each qualified employee. If the "qualified first-year wages" also qualified for the federal WOTC for vocational rehabilitation referrals, a credit is allowed for 35 percent of the first $6,000 in "qualified second-year wages" paid to each qualifying employee These credits would be applicable, but not limited, to employees that are veterans.

FISCAL IMPACT

If the bill is amended to resolve the implementation considerations addressed in this analysis, the department's costs are expected to be minor.

ECONOMIC IMPACT

Revenue Estimate

A revenue estimate is unable to be determined because the credit would be an unspecified percentage of qualified first year wages.

SUPPORT/OPPOSITION[4]

Support: None identified.

Opposition: None identified.

ARGUMENTS

Proponents: It could be argued that this bill would stimulate job creation by offering a tax incentive to businesses that have the ability to employ new workers and expand their current workforce.

Opponents: Some taxpayers may say that with the state's current fiscal crisis, additional tax expenditures should be avoided.

POLICY CONCERNS

Because this bill fails to specify otherwise, a taxpayer could claim the credit proposed by this bill, additional credits that the wages may qualify for, and a deduction for 100 percent of the wages the credit was based upon. Generally, a credit is allowed in lieu of any deduction or credit already allowable in order to eliminate multiple tax benefits.

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

LEGISLATIVE STAFF CONTACT

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[4] As reported on the Legislative Counsel's website at <http://www.leginfo.ca.gov/cgi-bin/postquery?bill_number=sb_1197&sess=CUR&house=B&author=calderon>[as of April 19, 2012].