

# ANALYSIS OF AMENDED BILL

## Franchise Tax Board

Author: Committee on Budget Analyst: Brian Werking Bill Number: AB 93  
Related Bills: See Legislative History Telephone: 845-5103 Amended Date: June 25, 2013  
Attorney: Patrick Kusiak Sponsor: \_\_\_\_\_

**SUBJECT:** Repeal Geographically Targeted Economic Development Area (G-TEDA) Incentives and New Jobs Tax Credit/Create Hiring Tax Credit/California Competes Tax Credit/Franchise Tax Board (FTB) Provide Annual Report to Joint Legislative Budget Committee Regarding Total Credits Claimed

### SUMMARY

This bill would do the following:

- Provision 1: Repeal the G-TEDA tax incentives and New Jobs Tax Credit under Personal Income Tax Law (PITL) and Corporation Tax Law (CTL).
- Provision 2: Create a New Hiring Tax Credit under PITL and CTL.
- Provision 3: Establish the California Competes Tax Credit Committee and create the California Competes Tax Credit under PITL and CTL.

This bill would also make changes to the Sales and Use Tax laws that are administered by the Board of Equalization. This analysis addresses only the provisions of the bill that would impact the FTB.

### RECOMMENDATION

No position.

### REASON FOR THE BILL

The reason for the bill is to address budgetary aspects of one of the state's largest and fastest growing tax expenditure programs, and provide additional tax incentive programs to encourage economic development.

### EFFECTIVE/OPERATIVE DATE

As an urgency measure, this bill would be effective immediately upon enactment. The operative dates of the provisions vary and are addressed separately for each provision.

Board Position:

\_\_\_\_\_ S      \_\_\_\_\_ NA        X   NP  
\_\_\_\_\_ SA      \_\_\_\_\_ O      \_\_\_\_\_ NAR  
\_\_\_\_\_ N      \_\_\_\_\_ OUA

Executive Officer

Date

Selvi Stanislaus

7/12/13

**ANALYSIS**

FEDERAL/STATE LAW

**PROVISION 1: Repeal the G-TEDA Tax Incentives and New Jobs Tax Credit.**

**EFFECTIVE/OPERATIVE DATE**

The provisions that would repeal the G-TEDA tax incentives would be specifically operative for transactions on or after January 1, 2014, and for taxable years beginning on or after January 1, 2014. The G-TEDA tax incentives, other than the hiring credits, would remain in effect until December 1, 2014, and as of that date would be repealed. The G-TEDA hiring tax credits would be operative for taxable years beginning before January 1, 2014, and for taxable years beginning on or after January 1, 2014, but only for employees hired within the 60 month period before January 1, 2014. The G-TEDA hiring credits remain in effect until December 1, 2019, and as of that date would be repealed. The New Jobs Tax Credit would specifically cease to be operative for taxable years beginning on or after January 1, 2014, and would be repealed on December 1, 2014.

**ANALYSIS**

STATE LAW

Tax Incentives

Under the Revenue and Taxation Code, existing state law provides a New Jobs Tax Credit of \$3,000 for each additional full-time employee hired for small businesses with 20 or fewer employees. In addition, existing state law provides special tax incentives for taxpayers conducting business activities within the G-TEDAs. These incentives include a hiring credit, sales or use tax credit, business expense deduction, and special net operating loss (NOL) treatment. Two additional incentives include net interest deduction for businesses that make loans to businesses within an Enterprise Zone (EZ) and a credit to taxpayers that are employees working in an EZ. The following table shows the tax incentives available to each of the G-TEDAs. Additional detail on the New Jobs Tax Credit and each of the G-TEDA tax incentives appear in Attachment A.

| G-TEDA Tax Incentives      | EZ | LAMBRA <sub>1</sub> | TTA <sup>2</sup> | MEA <sup>3</sup> |
|----------------------------|----|---------------------|------------------|------------------|
| Sales or Use Tax Credit    | X  | X                   | X                |                  |
| Hiring Tax Credit          | X  | X                   | X                | X                |
| Employee Wage Tax Credit   | X  |                     |                  |                  |
| Business Expense Deduction | X  | X                   | X                |                  |
| Net Interest Deduction     | X  |                     |                  |                  |
| Net Operating Loss         | X  | X                   | X                |                  |

<sup>1</sup> Local Agency Military Base Recovery Area (LAMBRA).

<sup>2</sup> Targeted Tax Area (TTA).

<sup>3</sup> Manufacturing Enhancement Area (MEA).

Carryover of Repealed or Inoperative Credits

For the carryover of credits that are repealed or become inoperative, California law provides that, unless otherwise provided, any remaining carryover of a credit that has been repealed or made inoperative shall continue to be allowed to be carried over in the same manner as was allowed immediately prior to that credit being repealed or becoming inoperative.<sup>4</sup>

THIS PROVISION

This provision would repeal the G-TEDA tax incentives listed in the chart above and repeal the New Jobs Tax Credit.

This provision would provide the following transition rules relating to the repeal of the G-TEDA hiring credits and sales and use tax credits:

- A portion of any hiring credit or sales and use tax credit remaining for carryover to taxable years beginning on or after January 1, 2014, if any, would be carried over only to the succeeding 10 taxable years until the credit is exhausted.
- Wages paid or incurred by a qualified taxpayer for employees first commencing employment with a qualified taxpayer within the 60-month period immediately preceding January 1, 2014, would continue to qualify as qualified wages for any remainder of the 60-month period for taxable years beginning on or after January 1, 2014.

IMPLEMENTATION CONSIDERATIONS

Implementing this provision can be done during normal annual updates without significant impact to the department.

**FISCAL IMPACT**

This provision would not significantly impact the department's costs.

**ECONOMIC IMPACT**

| Estimated Revenue Impact of AB 93<br>As Amended June 25, 2013<br>Provision 1: Repeal G-TEDA/New Jobs Tax Credit<br>For Taxable Years Beginning On Or After January 1, 2014<br>Assumed Enactment After June 30, 2013<br>(\$ in Millions) |         |         |         |
|---|---------|---------|---------|
| 2013-14   | 2014-15 | 2015-16 | 2016-17 |
| +\$109  | +\$411  | +\$713  | +\$858  |

This analysis does not account for changes in employment, personal income, or gross state product that could result from this provision.

<sup>4</sup> Revenue & Taxation Code sections 17039(d) and 23036(f).

## **PROVISION 2: Create a New Hiring Tax Credit**

### **EFFECTIVE/OPERATIVE DATE**

The provisions that would create a New Hiring Tax Credit would be specifically operative for taxable years beginning on or after January 1, 2014, and before January 1, 2021. The provisions that would authorize the New Hiring Tax Credit would remain in effect only until December 1, 2024, and as of that date would be repealed.

### **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.

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

State law provides that taxpayers operating in a G-TEDA are allowed a hiring credit for employing "qualified employees" during the first 60 months of employment. "Qualified employees" for the G-TEDA are defined by reference to various state and federal public assistance programs (Attachment B).

A qualified employee must be hired after the area is designated as an EZ 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 EZ and at least 50 percent must be performed inside the EZ. The business may claim up to 50 percent of the wages paid to a qualified employee during the first year, 40 percent during the second year, 30 percent during the third year, 20 percent during the fourth year, and 10 percent during the fifth year, as a credit against tax imposed on income from a trade or business operating within an EZ.

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.

The credit is recaptured if the qualified taxpayer terminates the qualified employee before the end of the longer of the following periods:

- The first 270 days of employment<sup>5</sup> (whether or not consecutive); or
- Ninety 90 days of employment<sup>6</sup> plus 270 calendar days.

---

<sup>5</sup> A day of employment includes any day the employee receives compensation including paid holidays, sick days, and vacation days.

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 Economic Development Area as the workplace of the employee) agency familiar with the public assistance statutes. The voucher is required to be retained by the qualified taxpayer in order for the certification to be made available to the FTB upon request.

### THIS PROVISION

This provision would create a New Hiring Tax Credit that would be available to a qualified taxpayer that hires a qualified full-time employee and pays or incurs qualified wages attributable to work performed by the qualified full-time employee in a designated census tract<sup>7</sup> or former EZ<sup>8</sup>. The qualified taxpayer must receive a tentative credit reservation from the FTB for that qualified full-time employee.

A qualified taxpayer means a person or entity engaged in a trade or business within a designated census tract or former EZ that during the taxable year pays or incurs qualified wages. A qualified taxpayer would be excluded from eligibility for the hiring credit if they provide services as described in the following codes or sectors of the North American Industry Classification System, unless the qualified taxpayer is a small business:

- Code 561320 Temporary Help Services
- Sector 44-45 Retail Trade
- Code 711110 Theater Companies and Dinner Theaters
- Code 722511 Full-Service Restaurants
- Code 722513 Limited-Service Restaurants
- Code 722514 Cafeterias, Grill Buffets, and Buffets
- Code 722515 Snack and Nonalcoholic Beverage Bars
- Code 713210 Casinos (except Casino Hotels)
- Code 721120 Casino Hotels
- Code 722410 Drinking Places (Alcoholic Beverages)

If a qualified taxpayer relocates to a designated census tract or former EZ from another location within the state, hiring credits would only be available if each employee at the previous location or locations is provided a written offer of employment with comparable compensation at the new location, unless the taxpayer is a small business<sup>9</sup>.

---

<sup>6</sup> *Ibid.*

<sup>7</sup> Would mean a census tract within the state that is determined by the Department of Finance to have a civilian unemployment rate that is within the top 25 percent of all census tracts within the state and has a poverty rate within the top 25 percent of all census tracts within the state.

<sup>8</sup> “Former enterprise zone” means an enterprise zone designated as of March 1, 2012, and any expansion of an enterprise zone prior to December 31, 2012, as in effect on December 31, 2012, excluding any census tract within an enterprise zone that is identified by the Department of Finance as a census tract with the lowest civilian unemployment and poverty.

<sup>9</sup> “Small business” means a trade or business that has aggregate gross receipts, less returns and allowances reportable to this state, of less than \$2,000,000 during the previous taxable year. For a partnership or “S” corporation the gross receipts limitation shall be applied to the partnership or the “S” corporation and to each partner or shareholder. For taxpayers required to be included in a combined report the gross receipts of those taxpayers as reported or authorized to be reported in a combined report.

A qualified full-time employee would mean an individual who meets all of the following requirements:

- Performs at least 50 percent of his or her services for the qualified taxpayer during the taxable year in a designated census tract or former EZ.
- Receives starting wages that are at least 150 percent of the minimum wage.
- Is hired by the qualified taxpayer on or after January 1, 2014.
- Is hired by the qualified taxpayer after the date the Department of Finance determines that the census tract is a designated census tract or that the census tracts within a former EZ are not census tracts with the lowest civilian unemployment and poverty.

A qualified full-time employee must satisfy either of the following conditions:

- Is paid qualified wages by the qualified taxpayer for services not less than an average of 35 hours per week.
- Is a salaried employee and was paid compensation during the taxpayer year for full-time by the qualified taxpayer.

Upon commencement of employment with the qualified taxpayer, the qualified employee must satisfy any of the following conditions:

- Was unemployed<sup>10,11</sup> for the six months immediately preceding commencement of employment with the qualified taxpayer.
- Is a veteran that has not been employed since separation from service in the Armed Forces of the United States.
- Was a recipient of the federal earned income tax credit for the previous taxable year.
- Was an ex-offender immediately preceding commencement of employment with the qualified taxpayer.

“Qualified wages” would mean those wages that meet all of the following requirements:

- That portion of wages paid or incurred by the qualified taxpayer during the taxable year to each qualified full-time employee that exceeds 150 percent of minimum wages, but does not exceed 350 percent of minimum wage.
- Wages paid or incurred during the 60-month period beginning with the first day the qualified full-time employee commences employment with the qualified taxpayer.

---

<sup>10</sup> An individual is “unemployed” for any period of time in which an individual is not in receipt of wages subject to state withholding, and not self employed, and not a registered full-time student at a high school, college, university, or other postsecondary educational institution for that period.

<sup>11</sup> In the case of a an individual that has completed a program of study at a college, university, or other postsecondary educational institution, received a baccalaureate, postgraduate, or professional degree, and was unemployed for six months immediately preceding employment with the qualified taxpayer, that individual must have completed that program of study at least 12 months prior to the individual’s commencement of employment with the qualified taxpayer.

The amount of the New Hiring Tax Credit allowable for a taxable year would be equal to the product of the tentative credit amount for the taxable year and the applicable percentage for that taxable year.

- The “tentative credit amount” for the taxable year would be equal to the product of the “applicable credit percentage” for each qualified full-time employee and the qualified wages paid by the qualified taxpayer during the taxable year to the qualified full-time employee. The “applicable credit percentage” for all calendar years would be 35 percent.
- The “applicable percentage” for a taxable year would be equal to a fraction, the numerator of which is the net increase in the total number of full-time employees in the state during the taxable year, determined on an annual full-time equivalent basis, as compared with the total number of full-time employees in the state during the base year, the denominator would be the total number of qualified full-time employees in the state during the taxable year. The applicable percentage may not exceed 100 percent.
  - “Base year” means the 2013 taxable year, except in the case of a qualified taxpayer who first hires a qualified full-time employee in a taxable year beginning on or after January 1, 2015, then the base year would mean the taxable year immediately preceding the taxpayer year in which the qualified full-time employee was first hired.
- The “net increase in full-time employees” would be determined as follows:
  - On an annual full-time equivalent basis, by subtracting the total number of full-time employees employed in the base year by the qualified taxpayer from the total number of full-time employees employed in the current taxable year by the qualified taxpayer.
  - For taxpayers who first commence doing business in this state during the taxable year, the number of full-time employees for the base year would be zero.

To be eligible for the credit a qualified taxpayer would be required to request a tentative credit reservation from the FTB within 30 days of complying with the Employment Development Department’s new hire reporting requirements, in a form and manner prescribed by the FTB. To obtain a credit reservation a taxpayer would provide necessary information to the FTB, including the name, social security number, the start date of employment, the rate of pay of the qualified full-time employee, the qualified taxpayer’s gross receipts from the previous taxable year, and whether the qualified full-time employee is a resident of a targeted employment area. A tentative credit reservation provided by the FTB to the qualified taxpayer would not constitute a determination by the FTB with respect to any of the requirements regarding a qualified taxpayer’s eligibility for the New Hiring Tax Credit.

A qualified taxpayer would be required to provide the FTB with an annual certification with respect to each qualified full-time employee hired in a previous taxable year, on or before the 15<sup>th</sup> day of the 3<sup>rd</sup> month of the taxable year.

The FTB would be required to do the following:

- Approve a tentative credit reservation request with respect to a qualified full-time employee hired during the calendar year.

- Determine the aggregate tentative reservation amount and the aggregate small business tentative reservation amount for a calendar year.
- Expeditiously process tentative credit reservation requests regarding qualified full-time employees that reside in a targeted employment area.
- Provide a searchable database for each taxable year beginning on or after January 1, 2014, and before January 1, 2019, that includes the employer names, amount of hiring tax credit claimed, and the number of new jobs created.
- Provide to the Joint Legislative Budget Committee an annual report regarding the amount of credits claimed during the previous fiscal year, by March 1, of each year.

The credit claimed by a qualified taxpayer in regards to a qualified full-time employee may be recaptured and assessed in the same manner as a mathematical error for the taxable year of termination if the qualified full-time employee is terminated by the qualified taxpayer at any time during the first 36 months, after commencing employment with the qualified taxpayer, unless any of the following occur:

- The qualified full-time employee voluntarily leaves the employment of the qualified taxpayer.
- The qualified employee becomes disabled and unable to perform the services of employment.
- The qualified employee was terminated for misconduct.
- The termination was due to a substantial reduction in the trade or business operations of the taxpayer, including reductions due to seasonal employment.
- The terminated qualified employee is replaced by other qualified full-time employees so as to create a net increase in both the number of employees and the hours of employment.

The New Hiring Tax Credit may only be claimed on a timely filed original return of the qualified taxpayer.

### IMPLEMENTATION CONSIDERATIONS

Implementing this provision would involve a new web based program to be established through which the taxpayer would be required to provide specific hiring data that would allow the department to issue a tentative credit reservation. This provision would also require the FTB to provide details about taxpayer credit usage through a searchable database. Costs associated with implementing this provision are detailed in the Fiscal Impact discussion below.

### **FISCAL IMPACT**

Staff estimates a first year cost of approximately \$800,000 and an ongoing cost of approximately \$400,000 to develop, program, and test, a web-based reservation system and to develop, program, and test a manually keyed searchable database.

**ECONOMIC IMPACT**

| Estimated Revenue Impact of AB 93<br>As Amended June 25, 2013<br>Provision 2: New Hiring Tax Credit<br>For Taxable Years Beginning On Or After January 1, 2014<br>Assumed Enactment After June 30, 2013<br>(\$ in Millions) |         |         |         |
|---|---------|---------|---------|
| 2013-14   | 2014-15 | 2015-16 | 2016-17 |
| -\$8.4  | -\$40.0 | -\$80.0 | -\$130  |

This analysis does not account for changes in employment, personal income, or gross state product that could result from this provision.

**PROVISION 3: Establish the California Competes Tax Credit Committee and Create the California Competes Tax Credit**

**EFFECTIVE/OPERATIVE DATE**

The provisions that would create the California Competes Tax Credit would be specifically operative for taxable years beginning on or after January 1, 2014, and before January 1, 2025. The provisions that would authorize the California Competes Tax Credit would remain in effect only until December 1, 2025, and as of that date would be repealed.

**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.

**THIS PROVISION**

This provision would establish the California Competes Tax Credit Committee (the “Committee”) comprised of the Treasurer, the Director of Finance, the Director of the Governor’s Office of Business and Economic Development (GO-Biz), or their representatives, and one appointee each from the Senate and the Assembly.

This provision would also create the California Competes Tax Credit. The amount of the credit available to a taxpayer for a taxable year would be negotiated and set forth in a written agreement between the GO-Biz and a taxpayer and would be based on the following factors:

- The number of jobs the taxpayer will create or retain in the state.
- The compensation paid or proposed to be paid by the taxpayer to its employees, including wages and fringe benefits.

- The amount of investment in this state by the taxpayer.
- The extent of unemployment or poverty in the area according to the United States Census in which the taxpayer's project or business is proposed or located.
- The incentives available to the taxpayer in the state, including incentives from the state, local government, and other entities.
- The incentives available to the taxpayer in other states.
- The duration of the proposed project and the duration the taxpayer commits to remain in the state.
- The overall economic impact in this state of the taxpayer's project or business.
- The strategic importance of the taxpayer's project or business to the state, region, or locality.
- The opportunity for future growth and expansion in the state by the taxpayer's business.
- The extent to which the anticipated benefit to the state exceeds the projected benefit to the taxpayer from the tax credit.

The written agreement between the GO-Biz and the taxpayer would include:

- Terms and conditions that include a minimum compensation level and a minimum job retention period.
- Provisions indicating whether the credit is to be allocated in full upon approval or in increments based on mutually agreed upon milestones when satisfactorily met by the taxpayer.
- Provisions that allow the Committee to recapture the credit, in whole or in part, if the taxpayer fails to fulfill the terms and conditions of the written agreement.

In negotiating a written agreement, the GO-Biz will give priority to a taxpayer whose project or business is located or proposed to be located in an area of high unemployment or poverty. Once a written agreement between the GO-Biz and a taxpayer has been negotiated, the GO-Biz would provide the agreement to the Committee for approval. The Committee would approve or reject any written agreement by resolution at a duly noticed public meeting.<sup>12</sup>

Upon approval of the written agreement by the Committee, the GO-Biz would inform the FTB of the terms and conditions of the written agreement. The FTB would review the books and records of taxpayers allocated a California Competes Tax Credit to ensure that the taxpayer complied with the terms and conditions of the written agreement. In the case of a small business, the FTB would review the books and records of the taxpayer if FTB deems the review appropriate or necessary in the best interest of the state. If the FTB determines that a possible breach of the agreement has occurred, the FTB would provide the GO-Biz detailed information regarding the basis of the possible breach.

---

<sup>12</sup> In accordance with the Bagley-Keene Open Meeting Act (Article 9 (commencing with Section 11120) of Chapter 1 of Part 1 of Division 3 of Title 2 of the Government Code).

The GO-Biz would then make a recommendation to recapture in whole or in part, the allocated tax credit, to the Committee. The Committee would approve or reject the recapture recommendation at a duly notice public meeting<sup>13</sup>.

The GO-Biz would then inform the FTB of any recapture of a previously allocated credit. The FTB would assess the amount of the recapture for the taxable year in which the Committee's recapture determination occurred, in the same manner as a mathematical error.<sup>14</sup>

The GO-Biz would post on its website all of the following:

- The name of each taxpayer allocated a California Competes Credit.
- The estimated amount of the investment by each taxpayer.
- The estimated number of jobs created or retained.
- The amount of the credit allocated to the taxpayer.
- The amount of the credit recaptured from the taxpayer, if applicable.

The aggregate amount of the credit that may be allocated in any fiscal year would be equal to \$30,000,000 for the 2013-14 fiscal year, \$150,000,000 for the 2014-15 fiscal year, and \$200,000,000 for each fiscal year from 2015-16 to 2018-19, inclusive. The amount available to be allocated in any given fiscal year may be adjusted if the amount available in a prior year was not allocated, or an amount allocated was recaptured, or if the Department of Finance determines that the amount allocated under this credit, the New Hiring Tax Credit, and manufacturing sales and use tax exemption exceeds \$750,000,000 in specified fiscal years.

For each fiscal year, 25 percent of the aggregate amount of the credit would be reserved for small businesses. No more than 20 percent of the aggregate amount of the credit may be allocated to a single taxpayer for each fiscal year.

#### IMPLEMENTATION CONSIDERATIONS

Implementing this provision will require the department to review contracts approved by the Committee and review the books and records of taxpayers allocated the California Competes Tax Credit. The costs associated with implementing this provision are detailed in the Fiscal Impact discussion below.

#### **FISCAL IMPACT**

Staff estimates a first year cost of approximately \$400,000 and an ongoing cost of approximately \$320,000 to review contracts approved by the Committee and review the books and records of taxpayers allocated the California Competes Tax Credit.

#### **ECONOMIC IMPACT**

In accordance with the bill provisions, staff defers to the Department of Finance for the estimated revenue loss for this credit.

---

<sup>13</sup> In accordance with the Bagley-Keene Open Meeting Act (Article 9 (commencing with Section 11120) of Chapter 1 of Part 1 of Division 3 of Title 2 of the Government Code).

<sup>14</sup> In the same manner as provided by Section 19051.

## LEGISLATIVE HISTORY

SB 434 (Hill, 2013/2014), among other things, would require a qualified taxpayer to have a net increase in full-time employees as compared to the taxpayer's base year before the taxpayer would be allowed to claim an EZ hiring credit. The amount of credit would relate directly to the ratio of the net increase in full-time employees to the number of qualified full-time employees employed during the year. SB 434 has been ordered to a third reading in the Senate.

SB 90 (Galgiani and Canella, Chapter 70, Statutes of 2013) modifies AB 93 as chaptered on July 11, 2013. Specifically, SB 90, for purposes of the new hiring tax credit, modifies the definition of qualified employee, excludes sexually oriented businesses from the definition of qualified taxpayer and small business, and modifies the defined geographical area that the hiring credit may be generated in.

AB 231 (Perez, 2011/2012), among other things, would have modified the definition of qualified wages within the EZ Hiring Credit to allow a greater portion of wages above the minimum wage to be used to calculate the credit and would have modified the definition of "qualified employee" to include additional categories of individuals. AB 231 failed to pass out of the Assembly by the constitutional deadline.

## SUPPORT/OPPOSITION

Support: None provided.

Opposition: None provided.

## ARGUMENTS

Proponents: Supporters could argue that the redirection of funds from the existing G-TEDA incentives to the new sales tax exemption, hiring credit, and California Competes Tax Credit will result in stronger job creation and retention within the state.

Opponents: Some could argue that economic investment and hiring decision making is often separate from tax planning decision making and because of this income tax hiring incentives are an inefficient way to encourage economic development.

## LEGISLATIVE STAFF CONTACT

Brian Werking

Legislative Analyst, FTB  
(916) 845-5103

[brian.werking@ftb.ca.gov](mailto:brian.werking@ftb.ca.gov)

Mandy Hayes

Revenue Manager, FTB  
(916) 845-5125

[mandy.hayes@ftb.ca.gov](mailto:mandy.hayes@ftb.ca.gov)

Jahna Carlson

Acting Asst. Legislative Director, FTB  
(916) 845-5683

[jahna.carlson@ftb.ca.gov](mailto:jahna.carlson@ftb.ca.gov)

## ATTACHMENT A

**New Jobs Tax Credit:** Under the Personal Income Tax Law (PITL) and the Corporate Tax Law (CTL), a tax credit of up to \$3,000 for each additional full-time employee hired is available to small businesses with 20 or fewer employees, beginning January 1, 2009. The credit is prorated on an annual full-time equivalent basis for employees employed less than a full year. To qualify, each qualified full-time hourly employee must be paid wages for not less than an average of 35 hours per week and each qualified full-time employee that is a salaried employee must be paid compensation during the year for full-time employment.

Generally, an employer may not claim the credit for those employees who are certified as a qualified employee in an EZ or similar incentive area, or for an employee whose wages are included in calculating any other credit allowed. In addition, there must be a net increase in qualified full-time employees compared to the number of full-time employees employed in the preceding taxable year. For taxpayers who first commence doing business in California during the taxable year, the number of qualified full-time employees considered employed in the preceding year would be generally be zero.

The credit is an allocated credit and the total amount of credit available to be claimed by all taxpayers is capped at \$400 million. The credit must be claimed on a timely filed original return received by the FTB on or before a cut-off date specified by the FTB. If the available credit exceeds the current year tax, any unused credit may be carried over to the next eight tax years or until the credit is exhausted, whichever occurs first.

**Sales or Use Tax Credit:** Taxpayers engaged in a trade or business within an EZ, LAMBRA, or TTA may take a credit equal to the Sales & Use Tax paid during the taxable year in connection with the purchase of qualified property. Qualified property includes specified machinery and machinery parts, data processing and communications equipment, and motion picture manufacturing equipment central to production and postproduction. The total cost of qualified property permitted for purposes of claiming this credit may not exceed \$1 million for PIT filers and \$20 million for CTL filers. Moreover, the qualified property must be used by the taxpayer exclusively in an EZ, LAMBRA, or TTA. Any unused portion of the credits may be carried over to succeeding taxable years until the credits are exhausted.

**Hiring Credit:** The largest G-TEDA incentive is the hiring credit. California law provides a credit to taxpayers that employ qualified employees in a G-TEDA during the taxable year equal to: (1) 50 percent of qualified wages in the first year of employment; (2) 40 percent of qualified wages in the second year of employment; (3) 30 percent of qualified wages in the third year of employment; (4) 20 percent of qualified wages in the fourth year of employment; and, (5) 10 percent of qualified wages in the fifth year of employment. In general, qualified wages means wages that do not exceed 150 percent of the minimum wage. Such wages must be paid to a qualified employee who works at least 90 percent of the time on activities directly related to the business located in a G-TEDA and whose services must be at least 50 percent performed within the boundaries of a G-TEDA. Qualified employees include economically disadvantaged individuals, dislocated workers, disabled individuals, ex-offenders, recipients of certain federal or state aid, members of a federally-recognized Indian tribes, or residents of a defined "targeted employment area" (TEA), where more than 50 percent of the residents are low- and moderate-

income. To qualify for the hiring credit, the taxpayer must obtain a certification, or voucher, indicating that the employee meets the eligibility criteria specified above. Taxpayers are required to retain a copy of this voucher and provide it upon request to the FTB. Any unused portion of the credits may be carried over to succeeding taxable years until the credits are exhausted.

**Employee Wage Credit:** Existing law allows a PIT credit equal to five percent of qualified wages, as defined, received by a qualified EZ employee during the taxable year. However, for each dollar of income received by the employee in excess of qualified wages, the credit is reduced by nine cents. Any unused portion of the credit may not be carried over to any taxable year.

**Business Expense Deduction:** Existing law allows taxpayers located in an EZ, LAMBRA, or TTA to treat 40 percent of the cost of specified property as an expense not chargeable to the taxpayer's capital account. Any such cost may be allowed as a deduction for the taxable year in which the taxpayer places the property in service. Such property must be for exclusive use in a trade or business conducted within an EZ, LAMBRA, or TTA.

**Net Interest Deduction:** California law provides for the deduction of net interest income on loans made to a trade or business located solely within an EZ. For purposes of the EZ net interest deduction, a qualified taxpayer (creditor) is defined as an entity that loans funds on or after the designation date of the EZ to a qualified business (debtor) and receives interest payments thereon. The taxpayer (creditor) does not have to be located in the EZ to take advantage of the net interest deduction; only the debtor needs to operate within the EZ.

**Net Operating Loss:** The G-TEDA net operating loss for taxpayers doing business in an EZ, LAMBRA, or TTA, allows 100 percent of a G-TEDA NOL, as defined, to be carried over for 20 years to reduce the amount of taxable EZ, LAMBRA, or TTA income in those years. The NOL carryover is determined by computing the business loss that results strictly from business activity in the specified G-TEDAs. G-TEDA NOL carryovers are allowed only for losses occurring in the tax year beginning after the date the area is designated as an enterprise zone.

## ATTACHMENT B

A qualified employee under the EZ hiring credit means an employee who qualified the taxpayer for the EZ hiring credit under former Section 17053.8 or the program area hiring credit under former Section 17053.11, or for purposes of all G-TEDA hiring credits, the qualified employees must meet any of the following criteria:

- Was a person eligible for services under the federal Job Training Partnership Act or its successor, who is receiving, or is eligible to receive, subsidized employment, training, or services funded by the federal Job Training Partnership Act, or its successor.
- Was a person eligible to be a voluntary or mandatory registrant under the Greater Avenues for Independence Act of 1985, or its successor.
- Was an economically disadvantaged individual 14 years of age or older.
- Was a disabled individual who is eligible for or enrolled in, or has completed a state rehabilitation plan or is a service-connected disabled veteran, veteran of the Vietnam era, or veteran who is recently separated from military service.
- Was an ex-offender. An individual shall be treated as convicted if he or she was placed on probation by a state court without a finding of guilt.
- Was a member of a federally recognized Indian tribe, band, or other group of Native American descent.
- Was a resident of a targeted employment area.
- Was a member of a targeted group, as defined in Section 51(d) of the Internal Revenue Code, or its successor.
- Was a dislocated worker who meets any of the following:
  - Has been terminated or laid off or who has received a notice of termination or layoff from employment, is eligible for or has exhausted entitlement to unemployment insurance benefits, and is unlikely to return to his or her previous industry or occupation.
  - Has been terminated or has received a notice of termination of employment as a result of any permanent closure or any substantial layoff at a plant, facility, or enterprise, including an individual who has not received written notification but whose employer has made a public announcement of the closure or layoff.
  - Is long-term unemployed and has limited opportunities for employment or reemployment in the same or a similar occupation in the area in which the individual resides, including an individual 55 years of age or older who may have substantial barriers to employment by reason of age.
  - Was self-employed (including farmers and ranchers) and is unemployed as a result of general economic conditions in the community in which he or she resides or because of natural disasters.
  - Was a civilian employee of the Department of Defense employed at a military installation being closed or realigned under the Defense Base Closure and Realignment Act of 1990.

- Was an active member of the armed forces or National Guard as of September 30, 1990, and was either involuntarily separated or separated pursuant to a special benefits program.
- Is a seasonal or migrant worker who experiences chronic seasonal unemployment and underemployment in the agriculture industry, aggravated by continual advancements in technology and mechanization.
- Has been terminated or laid off, or has received a notice of termination or layoff, as a consequence of compliance with the Clean Air Act.
- Was a person eligible for or a recipient of any of the following:
  - Federal Supplemental Security Income benefits.
  - Aid to Families with Dependent Children.
  - CalFresh benefits.
  - State and local general assistance.