Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author:	Steinberg	Analyst:	Jane Raboy	Bill Number:	SB 594
Related Bills:	See Legislative History	Telephone:	845-5718	Introduced Date:	February 22, 2013
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Career Pathways Investment Credit

SUMMARY

This bill would create a tax credit under the Personal Income Tax Law (PITL) and Corporation Tax Law (CTL) for taxpayers that provide career technical training in an amount allocated by the Career Pathways Investment Committee ("Committee").

This bill would also add provisions to the Education Code. The discussion of these changes is limited to the changes that would impact the department.

RECOMMENDATION

No position.

REASON FOR THE BILL

The reason for this bill is to reduce the secondary school dropout rate, create a highly skilled workforce, and encourage investment in career pathways programs.

EFFECTIVE/OPERATIVE DATE

This bill would become effective on January 1, 2014, and specifically operative for taxable years beginning on or after that date.

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.

Board Position:			Executive Officer	Date
______ S	______ NA	X NP		
______ SA	______ O	______ NAR	Selvi Stanislaus	4/19/13
______ N	______ OUA			

Existing federal or state law does not have a credit comparable to the one proposed in this bill.

Current state and federal laws generally allow taxpayers engaged in a trade or business to deduct all expenses that are considered ordinary and necessary in conducting that trade or business.

Corporate taxpayers who are members of a combined reporting group may make a one time, irrevocable assignment of earned tax credits to certain assignees eligible credits, as defined, to an eligible assignee, as defined, in taxable years beginning on or after July 1, 2008. Assigned credits can reduce tax for taxable years beginning on or after January 1, 2010.[1]

THIS BILL

This bill would allow a qualified taxpayer a nonrefundable tax credit in an amount equal to the amount allocated by the Committee as specified under the Education Code.

This bill would define a "qualified taxpayer," as an "applicant" as defined in the Education Code that is either the sole owner if an individual, partners if the taxpayer is a partnership or shareholders if the taxpayer is an "S" corporation that was awarded an allocation of the career pathways investment credit by the Committee.

The Committee would report to the Franchise Tax Board (FTB), once each year, the identity of the qualified taxpayers for whom the career pathways credits are allocated each year.

The amount of any unused tax credit may be carried over and used as a credit against the income tax liability in subsequent years until exhausted.

In the event that a qualified taxpayer fails to comply with the requirements set forth in this bill, the credit would be disallowed and assessed, and collected until the requirements are satisfied. A disallowed credit would be treated as a math error.

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.

The bill lacks administrative details that must be developed in order to implement the bill and determine its impacts to the department's systems, forms, and processes. For example:

- The bill lacks a certification process. Generally, credits that are allocated based on estimated expenditures are also subject to a certification process that would specify the responsibilities of a certifying agency, a department, and the taxpayer. For example, this bill is silent on who is responsible for certifying the actual expenditures the credit would be based upon and the form and manner the certifying agency would notify the taxpayer and the department of allocated and certified credits.

---
[1] Revenue and Taxation Code section 23663.

- The credit would be disallowed and assessed and collected "until the requirements are satisfied." By whom, how, and when would the department and taxpayers be notified of a taxpayer's noncompliance with the requirements? How and to whom would a taxpayer document that the requirements are subsequently satisfied? Would the credit be reinstated as a result of this documentation? Would the amount of the disallowed credit be subject to interest?

- Because this bill fails to specify otherwise, the CTL credit would be eligible for assignment. The bill is silent on whether and to what extent an assignee would become a party to the enforceable contract or memorandum of understanding required to obtain a credit allocation.

- The terms "applicant" and "taxpayer" are used interchangeably in defining "qualified taxpayer" in subdivision (b) of section 17057.6. This bill should be amended for consistency.

TECHNICAL CONSIDERATIONS

Subdivision (a) of Section 17057.6 needs to be amended where "Section 64204" appears, as the correct reference is "Section 64205."

Subdivision (b) of Section 17057.6 needs to be amended where "Section 64201 of the Education Code" appears, as the correct reference is "subdivision (a) of Section 64201 of the Education Code."

Subdivision (a) of Section 23610.6 needs to be amended where "Section 64204" appears, as the correct reference is "Section 64205."

Subdivision (b) of Section 23610.6 needs to be amended where "Section 64201 of the Education Code" appears, as the correct reference is "subdivision (a) of Section 64201 of the Education Code."

LEGISLATIVE HISTORY

SB 974 (Steinberg, 2009/2010) would have, among other things, established the Career Pathways Investment Credit. SB 974 failed to pass out of the Assembly by the constitutional deadline.

OTHER STATES' INFORMATION

Florida, Illinois, Massachusetts, Michigan, Minnesota, and *New York* laws do not provide a credit comparable to the credit allowed by this bill. The laws of these states were reviewed because their tax laws are similar to California's income tax laws.

FISCAL IMPACT

Department staff is unable to determine the costs to administer this bill until the implementation concerns have been resolved. As the bill continues to move through the legislative process and the implementation concerns are resolved, costs will be identified and an appropriation will be requested, if necessary.

ECONOMIC IMPACT

Until the implementation concerns have been resolved, the FTB is unable to determine the revenue impact of this bill.

LEGAL IMPACT

This bill would restrict this tax credit by providing priority to applicants that have entered into a contract or memorandum of understanding with local educational agencies, community colleges, or workforce investment boards in communities located within California. This bill could raise constitutional concerns under the Commerce Clause of the United States Constitution because it could appear to improperly favor in-state activity over out-of-state activity. On August 28, 2012, (*Cutler* v. Franchise Tax Board), the Court of Appeal issued a unanimous opinion holding that California's Qualified Small Business Stock statutes were unconstitutional. Specifically, the Court of Appeal held that the statutory scheme's requirement of a large California presence in order to qualify for an investment incentive discriminated against interstate commerce, and therefore violated the federal dormant commerce clause. While no court decision has yet invalidated, as a general matter, state income tax credits that provide an incentive for in-state activity, i.e., property placed in service in the state, employees employed in the state, etc., targeted tax credits such as the one proposed by this bill may be subject to constitutional challenge.

SUPPORT/OPPOSITION

Support: None provided.

Opposition: None provided.

ARGUMENTS

Proponents: Some may say that this bill would improve levels of preparation and academic skills, increase enrollment in postsecondary education, and facilitate entry into employment.

Opponents: Some may argue that a business is allowed to deduct ordinary and necessary expenses and additional incentives are unnecessary.

POLICY CONCERNS

This bill would allow a credit for qualified expenditures that are currently deductible as business expenses. For example, a taxpayer is generally allowed to deduct wages expense for internships, equipment purchase, or instructional materials in the normal course of business. This bill would allow the taxpayer to deduct these expenses while also claiming a credit on the tax return for the same expense. Generally, a credit is allowed in lieu of a deduction in order to eliminate multiple tax benefits for the same item of expense.

This bill would allow for an unlimited carryover period. Recent credits have been enacted with a carryover period limitation because experience shows credits typically are exhausted within eight years of being earned.

Generally, credits are limited as a percentage of amounts paid or incurred. This bill would allow a credit equal to 50 percent of the allocated amount without regard to any amount having been paid or incurred, which is unprecedented.

LEGISLATIVE STAFF CONTACT

Jane Raboy	Mandy Hayes	Jahna Carlson
Legislative Analyst, FTB	Revenue Manager, FTB	Acting Asst. Legislative Director, FTB
(916) 845-5718	(916) 845-5125	(916) 845-5683
jane.raboy@ftb.ca.gov	mandy.hayes@ftb.ca.gov	jahna.carlson.last@ftb.ca.gov