

BILL ANALYSIS

Department, Board, Or Commission Franchise Tax Board	Author Roth, et al.	Bill Number SB 718
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SUBJECT

Modify New Advanced Strategic Aircraft Tax Credit

SUMMARY

Among other things, this bill would, under the Corporation Tax Law, modify the previously enacted tax credit for certain taxpayers that hire employees to manufacture certain property for the United States Air Force.

This analysis discusses only the provisions of the bill that would impact the department.

REASON FOR THE BILL

The reason for the bill is to incentivize large manufacturing businesses to invest in California.

EFFECTIVE/OPERATIVE DATE

As an urgency measure, this bill would be effective and operative immediately upon enactment.

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.

For taxable years beginning on or after January 1, 2015, and before January 1, 2030, a taxpayer that is a major first-tier subcontractor awarded a subcontract to manufacture property for ultimate use in or as a component of a new advanced strategic aircraft for the United States Air Force is allowed a tax credit equal to 17 ½ percent of qualified wages paid or incurred during the taxable year to qualified full-time employees multiplied by an annual full-time equivalent ratio.

- “Qualified full-time employee” means an individual that is employed in this state by the qualified taxpayer and satisfies both of the following:
 - The individual’s services for the qualified taxpayer are at least 80 percent directly related to the qualified taxpayer’s subcontract to design, test, manufacture property, or otherwise support production of property for ultimate use in or as a component of a new advanced strategic aircraft for the United States Air Force.

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08/15/14

- The individual is paid compensation from the qualified taxpayer that satisfies either of the following conditions:
 - Was paid qualified wages for services of not less than an average of 35 hours per week, or
 - Was a salaried employee and was paid compensation during the taxable year for full-time employment.¹
- “Annual full-time equivalent ratio” means a ratio that cannot be greater than one, the numerator of which is 1,100 and the denominator of which is the number of qualified taxpayer’s qualified full-time employees computed on an annual full-time equivalent basis for the taxable year.
- “Annual full-time equivalent” means either:
 - In the case of an employee paid hourly, the total number of hours worked for the qualified taxpayer by the qualified employee divided by 2,000.
 - In the case of a salaried employee, the total number of weeks worked by the qualified employee for the qualified taxpayer divided by 52.
- “Qualified Wages” means wages paid or incurred by the qualified taxpayer during the taxable year with respect to qualified full-time employees that are direct labor costs², allocable to property manufactured in this state by the qualified taxpayer for ultimate use in or as a component of a new advanced strategic aircraft for the United States Air Force.
- “New advanced strategic aircraft for the US Air Force” means a new advanced strategic aircraft developed and produced for the United States Air Force under the New Advanced Strategic Aircraft Program.
- “New Advanced Strategic Aircraft Program” means the project designed to design, test, manufacture, or otherwise support production of a new advanced strategic aircraft for the United States Air Force under a contract that is expected to be awarded in the first or second calendar quarter of 2015.

The total aggregate amount of the credit that may be allowed to all taxpayers would be:

- In years one through five of the credit, the total aggregate amount allowed shall not exceed \$25,000,000 per calendar year.
- In years six through ten of the credit, the total aggregate amount allowed shall not exceed \$28,000,000 per calendar year.
- In years 11 through 15 of the credit, the total aggregate amount allowed shall not exceed \$31,000,000 per calendar year.

¹ Within the meaning of Section 515 of the Labor Code.

² Within the meaning of Section 263A of the Internal Revenue Code relating to capitalization and inclusion of inventory costs of certain expenses.

The credit is allocated on a first-come-first-served basis to the taxpayers that claim the credit on a timely filed original return.

Credit amounts in excess of the tax may be carried over for a maximum of eight years, if necessary, until exhausted.

The credit is in lieu of any other credit that is based on the same qualified wages.

No credit would be allowed unless the credit was reflected within the bid upon which the taxpayer's subcontract to manufacture property for the ultimate use in or as a component of a New Advanced Strategic Aircraft Program is based by reducing the amount of the bid by a good faith estimate of the allowable amount of the credit.

All reference to the credit and ultimate cost reductions incorporated into any successful bid that was awarded a subcontract for which a taxpayer is making claim, is required to be made available to the Franchise Tax Board (FTB) upon request.

THIS BILL

Effective immediately upon enactment, this bill would modify provisions of the newly enacted "Advanced Strategic Aircraft" tax credit as follows:

- Remove the "annual full-time employee ratio" calculation that had the effect of limiting the annual full-time equivalents for each taxpayer to 1,100.
- Modify one of the requirements in the definition of a "qualified full-time employee" to specify that the individual's services for the taxpayer must be performed in the state.
- Expand eligibility for the credit by modifying the definition of "qualified taxpayer" to include a prime contractor awarded a prime contract.
- Modify the definition of "New Advanced Strategic Aircraft Program" to exclude any contract awarded prior to August 1, 2014, and would not include a program to upgrade, modernize, sustain, or otherwise modify a current United States Air Force bomber program, including but not limited to the B-52, B-1, or B-2 programs.
- Modify the definition of "Total Annual Full-time Equivalents" to mean the number of qualified taxpayer's qualified full-time employees computed on an annual full-time equivalent basis for the taxable year.

Further, the bill adds the following requirements to the credit:

- The aggregate number of total annual full-time equivalents of all taxpayers for a calendar year could not exceed 1,100. This has the effect of retaining the 1,100 annual full-time equivalent limit, but applying it as an overall limit to all taxpayers claiming the credit.
- The FTB would be required to allocate the credit to taxpayers on a first-come-first-served basis, determined by the date the taxpayer's timely filed original tax return is received by the FTB. If the returns of two or more taxpayers are received on the same day and the amount of credit remaining to be allocated is insufficient to be allocated fully to each, the credit remaining would be allocated to those taxpayers on a pro-rata basis.

- The date a return is received would be determined by the FTB. The determination of the FTB as to the date a return is received and whether a return has been timely filed for purposes of the credit allocation would not be reviewable in any administrative or judicial proceeding.
- Any disallowance of a credit claimed due to the allocation limitations specified in this bill would be treated as a mathematical error appearing on the return. Any amount of tax resulting from that disallowance could be assessed by the FTB as a math error.³

IMPLEMENTATION CONSIDERATIONS

Implementing this bill would occur during the department's normal annual update.

LEGISLATIVE HISTORY

AB 2389 (Fox, et al., Chapter 116, Statutes of 2014), created the Advanced Strategic Aircraft tax credit that provides qualified employers a tax credit for certain wages paid to employees that work on an advanced strategic aircraft.

OTHER STATES' INFORMATION

Review of *Illinois, Florida, Massachusetts, Michigan, Minnesota, and New York* laws found no comparable tax credits. These states were selected and reviewed due to their similarities to California's economy, business entity types, and tax laws.

FISCAL IMPACT

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

ECONOMIC IMPACT

Revenue Estimate

Estimated Revenue Impact of SB 718 Assumed Enactment After June 30, 2014		
2014-15	2015-16	2016-17
\$ 0	\$ 0	\$ 0

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

³ A math error appearing on the return results in an assessment that is due and payable on notice and demand pursuant to R&TC Section 19051 instead of by a notice of proposed assessment with prepayment protest rights that generally is issued after an audit.

Revenue Discussion

This bill would modify the calculation of the Advanced Strategic Aircraft tax credit, but does not change the maximum annual allocation or estimated credit usage. Although the calculation of the credit has been changed, the department estimates the annual allocation cap would continue to be met. As such, there is no additional revenue loss associated with this bill.

APPOINTMENTS

None.

SUPPORT/OPPOSITION⁴

Support: Antelope Valley Board of Trade, Azusa Chamber of Commerce, City of El Segundo, City of Lancaster, City of Palmdale, City of Redondo Beach ,CONNECT, El Segundo Chamber of Commerce, Irwindale Chamber of Commerce, Lancaster Chamber of Commerce, Los Angeles Area Chamber of Commerce, Los Angeles County Economic Development Corporation, Manhattan Beach Chamber of Commerce, North San Diego Business Chamber, Northrop Grumman, Redondo Beach Chamber of Commerce and Visitors Bureau, San Diego Regional Chamber of Commerce, San Diego Regional Economic Development Corporation, San Gabriel Valley Economic Partnership, South Bay Association of Chambers of Commerce, Valley Industry and Commerce Association, West Valley-Warner Center Chamber of Commerce, and Yuba-Sutter Chamber of Commerce.

Opposition: None provided.

VOTES

	Date	Yes	No
Concurrence	08/13/14	32	4
Assembly Floor	08/11/14	75	0
Senate Floor	05/20/13	21	13

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⁴ As noted in the Senate Floor Analyses [sic] dated August 12, 2014.