Franchise Tax Board

ANALYSIS OF AMENDED BILL

Author:	Galgiani & Cannella	Analyst:	Brian Werking	Bill Number:	SB 90
Related Bills:	See Legislative History	Telephone:	845-5103	Amended Date:	July 2, 2013
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Clean-up Amendments to AB 93/New Hiring Tax Credit /California Competes Tax Credit

SUMMARY

This bill would provide clean-up provisions to the language of Assembly Bill 93 regarding the creation of the New Hiring Tax Credit, the creation of the new California Competes Tax Credit, and the sales and use tax exemption.

This analysis only addresses the provisions of the bill that would impact the Franchise Tax Board.

RECOMMENDATION

No position.

REASON FOR THE BILL

The reason for the bill is to provide clean-up language for AB 93 in order 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 provisions modifying the New Hiring Tax Credit would be operative for taxable years beginning on or after January 1, 2014, and before January 1, 2021. The provisions modifying the California Competes Tax Credit would be operative for taxable years beginning on or after January 1, 2014, and before January 1, 2025.

This bill would become operative only if AB 93 of the 2013-14 Regular Session is chaptered and becomes operative.

Board Position:			Executive Officer	Date
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ANALYSIS

BACKGROUND: AB 93 of the 2013-14 Regular Session

This bill would modify provisions of AB 93 of the 2013-14 Regular Session relating to the New Hiring Tax Credit and the California Competes Tax Credit. The provisions of AB 93 that would be modified are provided in this section for convenience. For a complete description of the provisions of AB 93, relating to the New Hiring Credit and the California Competes Tax Credit, see Appendix A.

New Hiring Tax Credit

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[1] or former Enterprise Zone[2] (EZ).

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)

[1] 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.
[2] "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.

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

- Was unemployed[3,4] 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.

California Competes Tax Credit

This provision would 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 Governor's Office of Business and Economic Development (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.

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[3] 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.

[4] 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 written agreement between The GO-Biz and the taxpayer would include the following:

- 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.

THIS BILL

This bill would, upon enactment, modify the provisions of the New Hiring Tax Credit and the California Competes Tax Credit as added by Assembly Bill 93 of the 2013-14 Regular Session, only if Assembly Bill 93 is also enacted.

New Hiring Tax Credit

This bill would modify the New Hiring Tax Credit provisions contained in AB 93 of the 2013-14 Regular Session as follows:

- Expand the geographic area that a qualified taxpayer would be required to be located in and in which a qualified full-time employee would be required to perform work, in order to qualify a taxpayer for the credit. Specifically, the geographic area would expand from only designated census tracts and former enterprise zones to designated census tracts and economic development areas. Economic development areas would include both former enterprise zones and LAMBRAs[5], as defined.
- Modify the definition of former enterprise zone to mean an enterprise zone designated and in effect as of December 31, 2011, any enterprise zone designated during 2012, and any revision of an enterprise zone prior to June 30, 2013, excluding any census tract within an enterprise zone that is identified by the Department of Finance pursuant to Section 13073.5 of the Government Code as a census tract within the lowest quartile of census tracts with the lowest civilian unemployment and poverty.
- Revise the ex-offender category in the definition of a qualified full-time employee. Ex-offender would be an ex-offender convicted of a felony, instead of the previous definition that would have included individuals that are placed on probation by a state court without a finding of guilt.
- Revise the veterans category in the definition of a qualified full-time employee. Veterans would be required to have separated from the military service within 12 months of commencing employment with a qualified taxpayer, in order to qualify as a qualified full-time employee.
- Add a new category to the definition of a qualified full-time employee—an individual that is a recipient of CalWORKS[6], as defined, or general assistance[7], as defined.

[5] Local agency military base recovery areas, in accordance with Section 7114 of the Government Code, that are designated as of the effective date of this bill.
[6] In accordance with Article 2 (commencing with Section 11250) of Chapter 2 of Part 3 of Division 9 of the Welfare Institutions Code.
[7] In accordance with Section 17000.5 of the Welfare and Institutions Code.

- Add a "sexually orientated business," as defined, to the list of employers that would not be considered a qualified taxpayer or a small business.

This bill would add provisions that would allow the GO-Biz to designate up to five designated pilot areas within designated census tracts and economic development areas that would allow a lower wage threshold for qualifying as qualified wages. The portion of wages of a qualified employee employed in a designated pilot area that is considered to be qualified wages would be that portion of wages paid or incurred by a qualified taxpayer between $10/hr and 350 percent[8] of the state minimum wage, instead of the portion paid or incurred between 150 percent[9] and 350 percent[10] of the state minimum wage for qualified employees employed designated census tracts or economic development area but outside of the designated pilot areas.

The designation of a designated pilot area would last for a period of four calendar years and could be extended by the GO-Biz for up to three additional calendar years, not to extend beyond December 31, 2020. The designation of the designated pilot areas and the extension of the designation is at the sole discretion of the GO-Biz and shall not be subject to administrative or judicial review.

California Competes Tax Credit

For purposes of the California Competes Tax Credit, this bill would specify that the credit be allocated by the GO-Biz for five fiscal years -- fiscal years 2013-14 through and including fiscal year 2017-18. The bill would also require that the amount of the credit that is allowed to be claimed for a taxable year or years, be set forth in the written agreement between the GO-Biz and the taxpayer.

This bill would provide off-code language that would clarify the changes made with respect to the carryover periods relating to the repealed Geographically Targeted Economic Development Area (G-TEDA) tax incentives and reiterate the application of existing law regarding the continuing availability of carryover credits after the repeal of each of the G-TEDA tax incentives made by Assembly Bill 93 of the 2013–14 Regular Session

IMPLEMENTATION CONSIDERATIONS

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

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.

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[8] $28/hr
[9] $12/hr
[10] $28/hr

AB 93 (Assembly Committee on Budget, Chapter 69, Statutes of 2013) repeals the geographically targeted economic development area tax incentives and the New Jobs Tax Credit under Personal Income Tax Law (PITL) and Corporation Tax Law (CTL), creates a New Hiring Tax Credit under PITL and CTL, establishes the California Competes Tax Credit Committee, and creates the California Competes Tax Credit under PITL and CTL.

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.

FISCAL IMPACT

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

ECONOMIC IMPACT

This bill, in conjunction with AB 93, would result in the following cumulative revenue losses:

Estimated Revenue Impact of SB 90 and AB 93 Cumulatively New Hiring Credit* For Taxable Years Beginning On or After January 1, 2014 Assumed Enactment After June 30, 2013 ($ in Millions)			
2013-14	2014-15	2015-16	2016-17
-$9	-$43	-$90	-$140

*This estimate does not include the revenue impact of the five "designated pilot areas". The bill provides that the Governor's Office is to designate the pilot areas based on criteria that numerous qualified census tracts and/or economic development areas meet. This could result in numerous different pilot areas, with numerous different anatomies. Because there is no way to predict which qualified census tracts and/or economic development areas will be a designated pilot area, the revenue impact of designated pilot area is unknown.

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

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 Hiring Tax Credit, and California Competes Tax Credit would 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, therefore, income tax hiring incentives are an inefficient way to encourage economic development.

LEGISLATIVE STAFF CONTACT

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APPENDIX A
PROVISIONS OF AB 93
NEW HIRING TAX CREDIT AND CALIFORNIA COMPETES TAX CREDIT

New Hiring Tax Credit

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[11] or former EZ[12]. The qualified taxpayer must receive a tentative credit reservation from the Franchise Tax Board (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[13].

[11] 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.
[12] "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.
[13] "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[14,15] 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.

[14] 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.

[15] 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 shall 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 15th day of the 3rd month.

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 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:

- 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.

California Competes Tax Credit

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.[16]

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.

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.[17]

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.[18]

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[16] 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).
[17] 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).
[18] In the same manner as provided by Section 19051.

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 2017-18, 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.