Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author:	Grove	Analyst:	Jessica Deitchman	Bill Number:	AB 1404
Related Bills:	See Legislative History	Telephone:	845-6310	Introduced Date:	February 27, 2015
		Attorney:	Bruce Langston	Sponsor	

SUBJECT:	Employer Hiring Credit/Employees with Disabilities

SUMMARY

This bill would, under the Personal Income Tax Law (PITL) and Corporation Tax Law (CTL), provide a tax credit for certain businesses that hire workers with disabilities.

RECOMMENDATION

No position.

REASON FOR THE BILL

The reason for the bill is to encourage employers to hire employees that may be paid a “special minimum wage” and to pay them at least the minimum wage.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2016.

PROGRAM BACKGROUND

The federal Fair Labor Standards Act[1] authorizes employers, after receiving a certificate from the Wage and Hour Division of the Federal Department of Labor to pay “special minimum wages” to workers who have disabilities for work being performed. Special minimum wage is less than minimum wage and is determined on a case by case basis.

FEDERAL/STATE LAW

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

[1] Section 14(c)

Board Position:						Executive Officer	Date
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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.

Current state law allows a New Employment Credit that is available to a qualified taxpayer that hires a qualified full-time employee, has an overall net increase in employment, and pays or incurs qualified wages attributable to work performed by the qualified full-time employee in a designated census tract[2] or former Enterprise Zone.[3] The qualified taxpayer must receive a tentative credit reservation from the Franchise Tax Board (FTB) for that qualified full-time employee.

THIS BILL

For taxable years beginning on or after January 1, 2016, under the PITL and CTL, this bill would allow a credit to a qualified employer who employs a qualified employee and pays the qualified employee a wage that equals or exceeds the minimum wage during the taxable year. The credit would be in an amount equal to the difference between the special minimum wage that may be paid to a qualified employee and the minimum wage.

The bill would define the following terms:

- "Minimum wage" means the wage established by the Industrial Welfare Commission.[4]
- "Qualified employee" means an individual who may be paid a special minimum wage, pursuant to Section 214 (c) of title 29 of the United States Code or Section 1191 or 1191.5 of the Labor Code.
- "Qualified employer" means a taxpayer that employs a qualified employee in this state.

In the case of any pass-thru entity, the determination of whether a taxpayer is a qualified employer under this bill would be made at the entity level and any credit under this bill would be allowed to the pass-thru entity and passed through to the partners or shareholders.[5]

- For purposes of this bill, the term "pass-thru entity" would mean any partnership or S Corporation.

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[2] 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.

[3] "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.

[4] As provided for in Chapter 1 of Part 4 of Division 2 of the Labor Code.

[5] In accordance with applicable provision of this part or part 11.

A qualified taxpayer would be required to do both of the following:

- Obtain from the Industrial Welfare Commission a certification that a qualified employee meets the eligibility requirements, as specified.
- Retain the certification and provide a copy of it upon request to the FTB.

IMPLEMENTATION CONSIDERATIONS

The department has identified the following implementation concerns. Department staff is available to work with the author's office to resolve these and other concerns that may be identified.

The credit would be equal to "the difference between the special minimum wage that may be paid to a qualified employee and the minimum wage." Generally minimum wage amounts, and hiring credits are expressed as a per-hour amount. As a result, the credit could be much lower than the author intends. If the author intends to allow credit based on total hours worked, this bill should be amended.

The bill fails to specify whether the federal or state special minimum wage would be controlling when both apply. The federal wage? The lower of the two wages? The higher? To avoid disputes between taxpayers and the department and to clearly express the author's intent, this bill should be amended.

The bill lacks detail on what should be included in the certificate provided. For ease of administration and certainty for taxpayers, it is recommended the bill be amended to require the certificate to prove the dollar amount of special minimum wage that may have been paid.

Because the bill fails to specify otherwise, the FTB would be subject to the rulemaking procedures required under the Administrative Procedures Act (APA).[6] Following these procedures may delay the immediate implementation of this bill. To prevent any delay, it is recommended that the author add a provision exempting the FTB from the APA when the FTB is prescribing rules, guideline, or procedures necessary or appropriate to carry out the purpose of this bill.

TECHNICAL CONSIDERATIONS

The definition of qualified employer on page 2, line 17, lacks quotation marks. For consistency among definitions, quotation marks are recommended.

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[6] Government Code section 11340 et seq.

Because an S-corporation is not a pass-thru entity for CTL purposes, the term "S-Corporation" on page 3, line 23, should be deleted.

LEGISLATIVE HISTORY

AB 236 (Swanson, 2011/2012) would have allowed a credit of $5,000 for each full-time employee hired that is either an ex-offender or has been unemployed for 12 consecutive months. AB 236 failed to pass out of the Assembly Appropriations by the constitutional deadline.

AB 304 (Knight, 2011/2012), would have allowed a credit of either $3,000 or $5,000 for each qualified employee that was paid wages greater than or equal to 200 percent of the average wage in the county in which the employee completes at least 50 percent of their work. AB 304 failed to pass out of the Assembly Revenue and Taxation Committee by the constitutional deadline.

AB 1009 (Wieckowski, 2011/2012) would have modified the former New Jobs Tax Credit to increase the allowance of the credit from employers with less than 20 employees to employers with 100 or less employees. AB 1009 failed to pass out of the Assembly Revenue and Taxation Committee by the constitutional deadline.

SB 156 (Emmerson/Cook, 2011/2012) would have modified the current New Jobs Tax Credit to increase the allowance of the credit from employers with less than 20 employees to employers with 50 or less employees. SB 156 failed to pass out of the Assembly Revenue and Taxation Committee by the constitutional deadline.

SB 640 (Runner, 2011/2012) would have allowed a credit of $500 per month (not to exceed 12 months) for each full-time employee hired who has received unemployment benefits for six months prior to being hired. SB 640 failed to pass out of the Assembly Revenue and Taxation Committee by the constitutional deadline.

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

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

ECONOMIC IMPACT

This bill would result in the following revenue loss:

Estimated Revenue Impact of AB 1404 As Introduced February 27, 2015 Assumed Enactment After June 30, 2015 ($ in Millions)		
2015-16	2016-17	2017-18
-22	-90	-170
This estimate assumes that the credit would be allowed for every hour that a qualified employee works for a qualified taxpayer.		

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

Revenue Discussion

The revenue impact of this bill would depend on the number of qualified disabled employed persons who are certified special minimum wage workers and are paid at least the prevailing minimum wage.

Using US Census Bureau data it is estimated that there would be 665,000 disabled employed persons in California in 2016. Based on statistics published by the US Department of Labor, it is estimated that 35 percent of California disabled individuals are certified special minimum wage workers. It is further assumed that 25 percent of these disabled persons work for for-profit entities that would claim this credit.

It was assumed that for-profit employers would learn about the new law and gradually increase wages paid to qualified employees. It is estimated that 20 percent would claim a credit in 2016, 50 percent in 2017, 85 percent in 2018, and 90 percent each year thereafter. It was assumed this bill would provide a small incentive for hiring disabled employees and the estimated number of qualified employees would increase 10 percent.

Using studies prepared by the GAO (United States General Accounting Office) on the special minimum wage, it was estimated the average special minimum wage worker would be paid 50 percent of California's minimum wage rate. Therefore, the taxpayer would earn a credit for the difference between the special minimum wage and the California minimum wage, for a tax credit equal to $5 per employee per hour of wages earned ($10 - $5 = $5). Assuming the qualified employee works 20-hour per week and 50 weeks per year, the total estimated tax credit generated would be $63 million in 2016, $160 million in 2017, and $220 million in 2018.

It was assumed that 80 percent of the credit amounts generated in each year would be used in that year due to a lack of sufficient tax liabilities.

The tax year estimates are converted to fiscal years, rounded, and reflected in the table above.

SUPPORT/OPPOSITION

Support: None provided.

Opposition: None provided.

ARGUMENTS

Proponents: Some may argue that this bill could increase the amount paid to employees that receive a "special minimum wage" by providing employers with a tax credit to encourage higher pay of these employees.

Opponents: Some may argue that providing a tax credit limited to employees that may be paid "special minimum wage" may be overly narrow and inadvertently exclude other groups of employees who could benefit from an incentive to pay higher wages.

POLICY CONCERNS

This bill would allow a credit for wages paid to a qualified employee that are currently deductible as business expenses. 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 fails to limit the amount of the credit that may be taken. Generally, credits are limited as a percentage of amounts paid or incurred. This bill would allow a 100 percent credit, which is unprecedented.

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

This bill lacks carryover language. As a result, any unused credit would be lost if the taxpayer is unable to use the entire credit amount in the year claimed. The author may wish to add language allowing a limited carryover period.

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