



Analysis of Original Bill

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Sponsor:

Bill Number: AB 3127

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Introduced: February 16, 2018

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Related Bills: See Legislative
History

Subject: Employer Wages Paid to Disabled Employees

Summary

This bill would, under the Personal Income Tax Law (PITL) and Corporation Tax Law (CTL), create an income tax credit for certain employers that hire employees eligible to be paid a “special minimum wage” and pay them at least the regular minimum wage.

Recommendation – No position.

Reason for the Bill

The reason for the bill is to encourage employers to employ individuals 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 operative immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2019, and before January 1, 2024.

PROGRAM BACKGROUND

The federal Fair Labor Standards Act¹ authorizes employers, after receiving a certificate from the Wage and Hour Division of the Federal Department of Labor, to pay a “special minimum wage” to individuals whose earning or productive capacity is impaired by age, physical or mental deficiency, or injury. A special minimum wage is less than the federal minimum wage and is determined on a case by case basis.

The California Labor Code² specifies that for any occupation in which a minimum wage has been established, the commission may issue to an employee who is mentally or physically handicapped, or both, a special license authorizing the employment of the licensee for a period

¹ Section 14(c) [29 U.S.C. §214(c)].

² Labor Code section 1191.

not to exceed one year from date of issue, at a wage less than the legal minimum wage. The commission shall fix a special minimum wage for the licensee. Such license may be renewed on a yearly 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.

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 or former Enterprise Zone. The qualified taxpayer must receive a tentative credit reservation from the Franchise Tax Board (FTB) for that qualified full-time employee.

As of January 1, 2019, California's minimum wage is generally \$11 per hour³ for those employers with 25 or fewer employees and \$12 per hour for those with 26 or more employees.

This Bill

For taxable years beginning on or after January 1, 2019, and before January 1, 2024, under the PITL and CTL, this bill would allow a credit to a qualified employer that pays a qualified employee a wage that equals or exceeds the state minimum wage during the taxable year. The credit would be in an amount equal to the difference between the special minimum wage paid or incurred to the qualified employee and the minimum wage, multiplied by the number of hours worked by the qualified employee for the qualified employer during the taxable year.

The bill would define the following terms:

- "Minimum wage" means the wage established by the Industrial Welfare Commission.
- "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, that is subject to withholding under the Unemployment Insurance Code.
- "Qualified employer" means a taxpayer that employs a qualified employee in this state.

³ Labor Code section 1182.12. Those employees classified as "learners" may be paid a lesser wage. See Labor Code section 1192. Additionally, those employees that are the parent, spouse, or child of the employer are not subject to the minimum wage requirement.

In the case of any pass-thru entity, the determination of whether a taxpayer is a qualified employer 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.

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

A qualified employer 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. The certification would include the dollar amount of special minimum wage applicable to each qualified employee.
- Retain the certification and provide a copy of it upon request to the FTB.

This bill would allow the FTB to prescribe rules, guidelines, or procedures necessary or appropriate to implement the credit and exempt from the requirements of the Administrative Procedure Act any standard, criterion, procedure, determination, rule, notice or guideline issued by the FTB.

Unused credits could be carried over for up to five years.

Any deduction otherwise allowed would be required to be reduced by the credit allowed.

On or before June 1, 2024, the FTB would be required to submit a report to the Legislature that contains the following:

- The number of Californians with developmental disabilities employed during each year this bill is operative,
- The number of employers who used and applied for a credit each year, and
- The number of employees for whom a credit was authorized by this bill was claimed.

The bill states that it is the intent of the legislature to comply with the provisions of Section 41.

This bill would remain in effect only until December 1, 2024, and would be repealed as of that date.

Implementation Considerations

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

The FTB would be required to report the number of Californians with developmental disabilities employed during the year. It is unclear how the FTB could determine this reporting requirement or whether another state agency currently gathers this information. It is recommended that this reporting requirement be removed or assigned to an appropriate state agency.

Legislative History

AB 1629 (Maienschein, 2017/2018) substantially similar to this bill, would have allowed a credit for employers that hire employees eligible to be paid a special minimum wage and chose to pay them at or above the minimum wage. AB 1629 failed to pass out of the Assembly by the constitutional deadline.

AB 1404 (Grove, 2015/2016) substantially similar to this bill, would have allowed a credit for employers that hire employees eligible to be paid a special minimum wage and chose to pay them at or above the minimum wage. AB 1404 failed to pass out of the house of origin by the constitutional deadline.

AB 2582 (Maienschein, 2015/2016) substantially similar to this bill, would have allowed a credit for employers that hire employees eligible to be paid a special minimum wage and chose to pay them at or above minimum wage. AB 2582 failed to pass out of the house of origin by the constitutional deadline.

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 Committee 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.

Other States' Information

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

Fiscal Impact

The department's costs to implement this bill have yet to be determined. As the bill moves through the legislative process, costs will be identified.

Economic Impact

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of AB 3127 as Introduced February 16, 2018
For Taxable Years Beginning On or After January 1, 2019
Assumed Enactment after June 30, 2018

(\$ in Millions)

Fiscal Year	Revenue
2018-2019	- \$1.3
2019-2020	- \$5.0
2020-2021	- \$10.0

This analysis does not account for changes in employment, personal income, or gross state product that could result from this bill or for the net final payment method of accrual.

Revenue Discussion

The revenue impact of this bill would depend on the number of California employers who have qualified employees who are certified special minimum wage workers and are paid the prevailing minimum wage in California.

Using US Department of Labor statistics for certificate holders, the number of workers paid special minimum wages in California would be approximately 20,900 in 2019. It is assumed that 10 percent of these disabled persons work for for-profit entities that would claim this credit. It is further assumed that for-profit employers would learn about the new law over time and gradually increase wages paid to qualified employees. It is estimated that, 20 percent of for-profit employers would generate a credit in 2019, 50 percent in 2020, 85 percent in 2021, and 90 percent each year thereafter. It is assumed this bill would provide a small incentive for hiring disabled employees and the estimated number of qualified employees would increase 10 percent each year.

Using studies prepared by the US General Accounting Office on the special minimum wage, it is estimated the average special minimum wage worker would be paid 50 percent of California's minimum wage rate. Under current California law, the minimum wage is scheduled to increase incrementally each year. The minimum wage in California would be \$12 in 2019, \$13 in 2020, and increase to \$15 by 2022. Taxpayers would earn a credit for the difference between the special minimum wage and the California minimum wage. In 2019, the average special minimum wage is estimated to be \$6.00 per hour. The estimated average credit would be equal to \$6.00 per employee per hour of wages earned ($\$12.00 - \$6.00 = \$6.00$). Assuming each qualified employee works 20 hours per week and 50 weeks per year, the total estimated tax credit generated would be \$2.8 million in 2019, \$7.8 million in 2020, and \$15 million in 2021.

It is assumed that 80 percent of the credit generated would be used in the year generated and the remaining credits would be used over the next several years. Adjustments were made to account for the offsetting tax effect of the reduced wage deduction that would be otherwise allowed under current law.

The tax-year estimates are converted to fiscal years and then rounded to arrive at the amounts reflected in the above table.

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” designation by providing employers with a tax credit to encourage higher pay for these employees.

Opponents: Some may argue that providing a tax credit limited to employees that may be paid a “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

The requirement that employees be located in this state may be interpreted to discourage intrastate commerce. Because the wages are already subject to California withholding, this requirement may be unnecessary.

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