STATE OF CALIFORNIA
Franchise Tax Board

Bill Analysis

Author: Gipson	Sponsor:	Bill Number: AB 1864
	Related Bills: See Legislative History	Introduced: February 8, 2022 Amended: March 24, 2022, and April 18, 2022

SUBJECT

Small Business Employer Local Hiring Tax Credit

SUMMARY

This bill would, under the Personal Income Tax Law (PITL) and the Corporation Tax Law (CTL), allow a tax credit to small business employers, as defined, for $434 per qualified employee.

RECOMMENDATION

No position.

SUMMARY OF AMENDMENTS

The March 24, 2022, amendments removed intent language relating to the support of small businesses and local governments by incentivizing local hires, and replaced them with the provisions discussed in this analysis.

The April 18, 2022, amendments inserted the credit amount of $434 per qualified employee.

This is the department's first analysis of the bill.

REASON FOR THE BILL

The reason for the bill is to incentivize small businesses to hire locally to retain critical revenue in local communities through the pandemic and onward and to provide a solution to high commuting.

ANALYSIS

For each taxable year beginning on or after January 1, 2023, and before January 1, 2028, this bill would allow a tax credit to qualified small business employers equal to $434 per qualified employee.

For purposes of this section, the following would apply:

1) A "qualified small business employer" would mean an employer that employs fewer than 49 employees on average at any time during the taxable year.
2) A "qualified small business employer" would not include a public employer. A "public employer" would mean:
   i. The state and every state entity, including, but not limited to, the Legislature, the judicial branch, the University of California, and the California State University.
   ii. A political subdivision of the state, or agency or instrumentality of the state or subdivision of the state, including, but not limited to, a city, county, city and county, charter city, charter county, school district, community college district, joint powers authority, joint powers agency, and any public agency, authority, board, commission, or district.
3) A "Qualified employee" would mean an employee of the qualified small business employer who is performing services for the employer in this state and who meets all of the following requirements:
   i. The employee is full-time, as designated by the employer.
   ii. The employee's permanent place of residence is within a five-mile radius of the employee's primary worksite.
   iii. The employee has worked for the employer for at least 6 months but less than 18 months at the time the credit is claimed.

The qualified small business employer would be limited to one credit for each qualified employee regardless of whether the employee is rehired.

Unused credits could be carried over to subsequent taxable years until exhausted.

As the bill does not specify otherwise, this credit would not reduce regular tax below the tentative minimum tax.

For the purposes of Revenue and Taxation Code (RTC) section 41, this bill provides that the Legislature's specific goal, purpose, and objective is to provide support to small businesses by incentivizing local hires. Detailed performance indicators to determine whether these credits meet the goal, purpose, and objective would include the number of small business employers who utilized the credits, the number of qualified employees hired, and the total dollar amount of credits claimed.

The Franchise Tax Board (FTB) would be required to analyze the performance indicators for each taxable year and report the findings to the Legislature on or before January 1, 2027, in compliance with the Legislative reporting requirements under Government Code section 9795. In addition, the reporting requirements would be treated as an exception to the disclosure rules under Section 19542.

This credit would be repealed by its own terms on December 1, 2028.

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, 2023, and before January 1, 2028.

Federal/State Law

Federal Law

The American Rescue Plan Act of 2021 (ARPA), provides eligible employers a refundable tax credit against employment taxes to reimburse them for the cost of providing sick leave to employees unable to work or telework due to a COVID-19 quarantine order, advice to self-quarantine, for experiencing COVID-19 symptoms and seeking a medical diagnosis, awaiting results of a test or diagnosis of COVID-19 when exposed or when the employer requests the test or diagnosis, obtaining COVID-19 immunization, or recovering from injury or illness from a COVID-19 immunization.

Eligible employers are those with fewer than 500 employees and certain governmental employers. Employers are allowed a sick leave credit of up to 80 hours, at a maximum of $511 per day, but no more than $5,110 per employee in total, plus related health care costs. The credit was allowed for wages paid on April 1, 2021, through September 30, 2021.

State Law

Existing state 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 hiring credits). These credits generally are designed to provide incentives for taxpayers to perform various actions or activities that they may not otherwise undertake.

The Main Street Small Business Tax Credit, for the taxable year beginning on or after January 1, 2020, and before January 1, 2021, under the Sales and Use Tax Law (SUTL), the PITL and the CTL, allowed a small business hiring credit to a qualified small business employer that received a tentative credit reservation under RTC section 6902.8, equal to $1,000 for each net increase in qualified employees, as specified. The credit could not exceed $100,000 for any qualified small business employer. In lieu of the credit under the PITL or CTL, an irrevocable election could be made to apply the credit amount against qualified sales or use taxes (SUT), as specified. These tax credits were repealed by their own terms on December 1, 2021.

The Main Street Small Business Tax Credit, Part II, for the taxable year beginning on or after January 1, 2021, and before January 1, 2022, under the SUTL, the PITL and the CTL, allows a small business hiring credit to a qualified small business employer that received a tentative credit reservation under RTC section 6902.10. A tentative credit reservation amount could be an amount equal to $1,000 for each net increase in qualified employees, as specified, not to exceed $150,000 for any qualified small business employer. In lieu of the credit under the PITL or CTL, an irrevocable election can be made to apply the credit amount against qualified SUT, as specified. These tax credits will be repealed by their own terms on December 1, 2022.

Under RTC section 41, legislation that would create a new tax expenditure is required to include specific goals, purposes, objectives, and performance measures to allow the Legislature to evaluate the effectiveness of the credit.

Implementation Considerations

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

The definition of a qualified small business employer is an employer that employs fewer than 49 employees "on average at any time" during the taxable year. The term "on average" conflicts with the term "at any time." For clarity, the author may wish to amend the bill to remove the term "on average," "at any time," or "on average at any time" from the definition.

This bill would require the department to provide a report on the utilization of this credit by January 1, 2027. However, the department would not have the data for all taxable years by the required reporting date. The earliest the FTB could provide complete data for a tax year is generally one year after the original due date for individual returns, and one year after the extended due date for corporation returns. For example, for corporations, the extended due date for the 2027 taxable year would generally be November 15, 2028, meaning the FTB would not have complete data until at least November 2029. The author may wish to amend the bill to extend the due date of the reporting requirements to report by December 2029 to allow the department to collect and report the data for all taxable years.

Technical Considerations

For consistency of terminology, the following changes are recommended:

1. Section 17053.82 (b)(2)(C) replace, "The employee has worked for the employer for at least 6 months but less than 18 months at the time the credit is claimed." with "The employee has worked for the employer for at least 6 months but less than 18 months at the time *the return is filed.*"
2. Section 23682 (b)(2)(C) replace, "The employee has worked for the employer for at least 6 months but less than 18 months at the time the credit is claimed." with "The employee has worked for the employer for at least 6 months but less than 18 months at the time *the return is filed.*"

Policy Considerations

A qualified employee would be required to be "full-time, as designated by the employer." Because employers may define a "full-time" employee differently, generally the statute would specifically define "full-time" as a specific number of hours. The author may wish to amend the bill to define the term.

This bill would allow for an unlimited carryover period of the unused credits. Consequently, the department would be required to retain the carryover on the tax forms indefinitely. Credits are generally enacted with a limited carryover period because experience shows that credits typically are exhausted within eight years of being earned.

This bill would allow a credit for qualified expenditures 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. Providing both a credit and allowing the full amount to be deducted would have the effect of providing a double benefit for that item. The author may wish to amend to the bill to provide that a deduction would not be allowed for any amount taken into account in the computation of these credits.

LEGISLATIVE HISTORY

AB 62 (Gray, 2021/2022), under the PITL and the CTL, would have created a credit for the total amount paid or incurred by a qualified taxpayer to comply with regulations adopted by Occupational Safety and Health Standards Board, relating to COVID-19 prevention. AB 62 did not pass out of the Assembly Revenue and Taxation Committee by the constitutional deadline.

AB 1890 (Choi, et al., 2021/2022) would, under the PITL and the CTL, allow a tax credit to employers that paid COVID-19 SPSL for taxable years beginning on or after January 1, 2021, and before January 1, 2023. AB 1890 is in the committee process with the Assembly Revenue and Taxation Committee.

AB 1920 (Fong, 2021/2022) would, under the PITL and the CTL, allow a tax credit to employers that paid COVID-19 SPSL for taxable years beginning on or after January 1, 2022, and before January 1, 2023. AB 1920 is in the committee process with the Assembly Revenue and Taxation Committee.

AB 150 (Committee on Budget, Chapter 82, Statutes of 2021), among other things, for the taxable year beginning on or after January 1, 2021, and before January 1, 2022, under the SUTL, the PITL, and the CTL, allowed the Main Street Small Business Tax Credit, Part II, to qualified small business employers a small business hiring credit, subject to receiving a tentative credit reservation. The amount of the credit is reduced if the qualified small business employer received a tentative credit reservation amount under RTC section 6902.8.

SB 1447 (Bradford, et al., Chapter 41, Statutes of 2020), under the SUTL, PITL and the CTL, allowed the Main Street Business Tax Credit to qualified small business employers a small business hiring credit, subject to receiving a tentative credit reservation. In lieu of the credit under the PITL or CTL, an irrevocable election could be made to apply the credit amount against qualified SUT, as specified.

AB 1842 (Salas, 2019/2020), under the PITL and the CTL, would have, among other things, created the COVID-19 Small Business/Nonprofit Tax Credit. AB 1842 did not pass out of the Assembly Judiciary Committee by the constitutional deadline.

PROGRAM BACKGROUND

None noted.

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 1864 as Amended April 18, 2022
Assumed Enactment after June 30, 2022

($ in Millions)

Fiscal Year	Revenue
2022-2023	-$34
2023-2024	-$75
2024-2025	-$90

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.

LEGAL IMPACT

None noted.

APPOINTMENTS

None noted.

SUPPORT/OPPOSITION

To be determined.

ARGUMENTS

To be determined.

LEGISLATIVE CONTACT

FTBLegislativeServices@ftb.ca.gov