STATE OF CALIFORNIA
Franchise Tax Board

Bill Analysis

Author: Caballero & Villapudua	Sponsor:	Bill Number: SB 1349
	Related Bills: See Legislative History	Amended: May 19, 2022, June 13, 2022, & June 28, 2022

SUBJECT

California New Employment Credit

SUMMARY

This bill would, under the Personal Income Tax Law (PITL) and Corporation Tax Law (CTL), modify the existing New Employment Credit (NEC) to remove the requirement that work be performed in a designated census tract or economic development area, remove all requirements relating to those designated areas, expand the definition of a qualified full-time employee, add Section 41 language, add a tax levy provision, and make other technical nonsubstantive changes.

RECOMMENDATION

No position.

SUMMARY OF AMENDMENTS

The May 19, 2022, amendments removed the provisions of the bill related to the California Work Opportunity Credit and replaced them with the provisions discussed in this analysis.

The June 13, 2022, amendments modified the definition of a qualified taxpayer to allow certain previously excluded employers to qualify for the credit.

The June 28, 2022, amendments modified the definitions of a qualified full-time employee, qualified taxpayer, and qualified wages and added a provision regarding the aggregate credit limitation.

REASON FOR THE BILL

The reason for the bill is to broaden the NEC and help reduce unemployment within targeted groups by eliminating the designated geographic areas requirement and expanding the eligibility criteria.

ANALYSIS

This bill would, for taxable years beginning on or after January 1, 2023, modify the NEC by removing the requirement that the work performed by the qualified full-time employee be in a designated census tract or economic development area.

This bill would remove all definitions, requirements, and references to a designated census tract or economic development area.

Additionally, this bill would modify the definition of a qualified full-time employee to:

- Remove the requirement that at least 50% of services be performed in a designated census tract or economic development area.
- Update the hired by date to apply the revisions made by this bill from "on or after January 1, 2014," to "on or after January 1, 2023."
- Expand eligibility to an employee if a qualified taxpayer claimed a federal work opportunity credit during the taxable year for the employee on the qualified taxpayer's federal income tax return. For purposes of this credit, the federal work opportunity credit would mean the work opportunity tax credit (WOTC) under Section 51 of the Internal Revenue Code (IRC) for wages paid or incurred by the qualified taxpayer to qualified individuals as specified.

This bill would provide that an individual that is considered, and is claimed by a qualified taxpayer as a qualified full-time employee for any taxable year beginning before January 1, 2023, under the previous version of this law, would continue to be considered a "qualified full-time employee" for the period of time commencing with the date the individual is first employed by the qualified taxpayer and ending 60 months thereafter if the individual continues to be paid, or the qualified taxpayer incurs for the individual, qualified wages, as specified. Notwithstanding other provisions in this section, however, these qualified wages would not be required to be subject to withholding under the Unemployment Insurance Code.

This bill would modify the definition of qualified wages by removing the requirement that qualified full-time employees be employed in a designated pilot area, and remove the definition of designated pilot areas and all references to the computation of the credit specific to pilot areas.

"Wages" would mean wages subject to withholding under the Unemployment Insurance Code.

This bill would remove the provision requiring the Department of Finance (DOF) to provide the Franchise Tax Board (FTB) with a list of the designated census tracts and a list of census tracts with the lowest civilian unemployment rate.

Furthermore, this bill would remove the provision requiring the DOF to estimate the total dollar amount of credits that will be claimed under this section with respect to each fiscal year from the 2013–2014 fiscal year to the 2020–2021 fiscal year, inclusive.

This bill would provide the requirements of the credit reservation system would not be construed to limit the aggregate amount of credits granted to all qualified taxpayers.

This bill would add language to the existing FTB annual reporting requirements stating that the report was for purposes of complying with Section 41.

In addition, this bill states that for purposes of complying with Section 41, the Legislature finds and declares that the goal, purpose, and objective of the tax expenditure, as amended by this bill, is to encourage and expand the hiring of qualified employees in the state by providing a credit for jobs that will provide a living wage and opportunities for California residents. The bill lists the following detailed performance indicator:

- The total dollar amount of the credits claimed.

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, 2026.

Federal/State Law

Federal Law

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

The WOTC is a federal income tax credit available to employers who hire and retain individuals from specified targeted groups who have consistently faced significant barriers to employment. Employers must apply for and receive a certification verifying the new hire is a member of a targeted group before they can claim the tax credit. After the required certification is secured, taxable employers claim the WOTC as a general business credit against their income taxes, and tax-exempt employers claim the WOTC against their payroll taxes. The credit is unavailable for wages paid to employers that begin work after December 31, 2025.

State Law

For taxable years beginning on or after January 1, 2014, and before January 1, 2026, current state law allows a NEC 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 economic development area. The qualified taxpayer must receive a tentative credit reservation from the FTB for that qualified full-time employee. Additionally, the FTB must provide a searchable database on its website reporting the name of the person or entity claiming 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.

This bill would continue to require the FTB to provide as a searchable database on its internet website, for each taxable year beginning on or after January 1, 2014, and before January 1, 2026, the employer names, amounts of tax credit claimed, and number of new jobs created for each taxable year. The expansion of the NEC as provided for in this bill could result in an increase in the number of taxpayers claiming this credit. Accordingly, the cost to publish a searchable database containing the employer names, amounts of tax credit claimed, and number of new jobs created could also increase, as indicated below in "Fiscal Impact." The author may wish to consider amending the bill to modify the searchable database requirement, taking into account the potential increase in the population expected as a result of the provisions in this bill.

Technical Considerations

The bill would continue to require the FTB to annually provide to the Joint Legislative Budget Committee, by no later than March 1, a report of the total dollar amount of the credits claimed under this section with respect to the relevant fiscal year. The report is required to compare the total dollar amount of credits claimed with respect to that fiscal year with the department's estimate. Further, if the total dollar amount of credits claimed for the fiscal year is less than the estimate for that fiscal year, the report is required to identify options for increasing annual claims of the credit so as to meet estimated amounts. However, this bill would remove DOF's requirement to estimate the total dollar amount of credits that will be claimed with respect to each fiscal year. Without this estimate, FTB cannot meet the above reporting requirement. The author may wish to amend the bill to remove the particular requirement to compare the total dollar amount of credits claimed with respect to that fiscal year with the department's estimate.

Policy Considerations

Existing law requires that the credit be claimed on a timely filed original return of the qualified taxpayer and only with respect to a qualified full-time employee for whom the qualified taxpayer has received a tentative credit reservation. The tentative credit reservation requirement serves the purpose of preventing taxpayers without a reservation from claiming the credit. Allowing a qualified taxpayer that received a reservation to claim the credit on an amended return would provide additional time to claim the credit if a qualified taxpayer did not have an opportunity to claim the credit on their original return. The author may wish to amend the bill to remove the timely filed original return requirement.

LEGISLATIVE HISTORY

AB 2035 (Villapudua, 2021/2022) would have amended the existing NEC to expand eligibility to additional industries similar to SB 1349 and extended the pilot area designation period. AB 2035 did not pass out of the house of origin by the constitutional deadline.

AB 3029 (Arambula, 2017/2018) would have amended the existing NEC to remove the FTB's responsibility to provide a searchable database on its website and create the California New Employment Credit (California NEC). AB 3029 did not pass out of the house of origin by the constitutional deadline.

SB 661 (Fuller, 2017/2018) would have expanded the NEC by adding a new type of qualified employee. SB 661 did not pass out of the house of origin by the constitutional deadline.

SB 90 (Galgiani and Canella, Chapter 70, Statutes of 2013), modified AB 93 as chaptered on July 11, 2013. Specifically, SB 90, for purposes of the NEC, modified the definition of qualified employee, excluded sexually oriented businesses from the definition of qualified taxpayer and small business, and modified the defined geographical area that the hiring credit may be generated in.

AB 93 (Assembly Committee on Budget, Chapter 69, Statutes of 2013), repealed the geographically targeted economic development area tax incentives and the New Jobs Tax Credit under the PITL and CTL, created a NEC, established the California Competes Tax Credit (CCTC) Committee, and created the CCTC under the PITL and CTL.

PROGRAM BACKGROUND

The NEC Program was created in 2014 to promote employment for businesses that operate in areas with historically high unemployment and high poverty rates. The NEC 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.

The NEC will be repealed on December 1, 2029.

FISCAL IMPACT

The department's costs to implement this bill for the first year are expected to be minimal. For the following years, the costs to maintain the searchable database specified in the statute due to the credit expansion are as follows: $350,000 for fiscal year 2024-2025; and estimated on-going annual costs ranging between $120,000 and $310,000. The department will pursue a budget change proposal if necessary.

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of SB 1349 as Amended on June 28, 2022
Assumed Enactment after June 30, 2022

($ in Millions)

Fiscal Year	Revenue
2022-2023	-$2.6
2023-2024	-$5.6
2024-2025	-$7.3

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

Based on FTB NEC data, industry employment data, California Work Opportunity Tax Credit data from the Employee Development Department, and wage data from the U.S. Bureau of Labor Statistics, it is estimated that an additional 1.9 million employees would be eligible for the expanded NEC. Based on FTB NEC data trends, it is estimated that approximately 65,000, or 3 percent of eligible employees would be claimed and used in the computation of the credit. Based on this information, it is estimated that this credit expansion would result in a revenue loss of approximately $4.8 million in the 2023 taxable year.

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

LEGAL IMPACT

None noted.

APPOINTMENTS

None noted.

SUPPORT/OPPOSITION

Support

National Federation of Independent Business

Opposition

California Teachers Association

ARGUMENTS

As per the Assembly Appropriations Committee analysis of SB 1349, dated August 9, 2022, the following support and opposition of the bill is presented:

Proponents

> This bill is supported by business groups such as the National Federation of Independent Business, which notes, "by melding elements of WOTC with NEC, the law will provide a simplified process for employers to qualify for the tax credit."

Opponents

This bill is opposed by the California Teachers Association because the reduction in revenue lowers Proposition 98 education funding in the state budget.

LEGISLATIVE CONTACT

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