STATE OF CALIFORNIA
Franchise Tax Board

Bill Analysis

Author: Limón	Sponsor:	Bill Number: SB 553
	Related Bills: See Legislative History	Amended: March 10, 2021, and April 15, 2021

SUBJECT

California Work Opportunity Tax Credit

SUMMARY

This bill would, under the Personal Income Tax Law (PITL) and the Corporation Tax Law (CTL), provide a tax credit to certain employers that hire employees who are members of a targeted group.

RECOMMENDATION

No position.

SUMMARY OF AMENDMENTS

The March 10, 2021, amendments deleted the introduced intent language and added Legislative intent language about the purpose of the California Work Opportunity Credit (WOTC) and the PITL and CTL provisions for the WOTC.

The April 15, 2021, amendments revised the date of the federal WOTC definition of wages, include new revisions to the federal WOTC, and made other technical changes.

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

REASON FOR THE BILL

The reason for the bill is to encourage the hiring of targeted group employees by offering a tax credit.

ANALYSIS

This bill would, under the PITL and CTL, for taxable years beginning on or after January 1, 2021, and before January 1, 2025, allow a qualified employer, a California WOTC in an amount determined in accordance with the federal WOTC, as applicable for federal tax purposes for the taxable year.

The bill would specify a calculation of the credit as follows:

- Allow a credit equal to 40 percent of the amount of wages paid by a qualified employer to a qualified individual in the first year.
- The credit amount would be limited to $2,400 per qualified individual.
- The first $5,000 of wages paid to a qualified individual are excluded from the calculation of the credit.
- The wages are required to be attributable to an employee from a targeted group, who has worked at least 500 hours for the qualified taxpayer.

The bill would define the following terms and phrases:

- "California WOTC" means the California work opportunity tax credit.
- "Federal WOTC" means the federal work opportunity tax credit allowed by Section 51 of the Internal Revenue Code (IRC) as in effect on January 1, 2021.
- "Qualified employer" means a taxpayer that is an employer that is subject to, and is required to provide, unemployment insurance to the taxpayer's employees pursuant to the Unemployment Insurance Code.
- "Qualified individual" means any person who is covered by the unemployment insurance by his or her employer pursuant to the Unemployment Insurance Code.
- "Wages" means those wages subject to withholding of the Unemployment Insurance Code.

The bill would allow a credit for wages paid to an employee that is a member of the following targeted groups:

- A qualified IV-A recipient
- A qualified veteran
- A qualified ex-felon
- A vocational rehabilitation referral
- A qualified supplemental nutrition assistance program benefits recipient
- A qualified SSI recipient
- A long-term family assistance recipient
- A qualified long-term unemployment recipient

However, wages paid within these targeted groups would be ineligible for the credit if the employee is:

- o A qualified veteran who is certified by the designated local agency as having aggregate periods of unemployment during the one-year period ending on the hiring date which equal or exceed four weeks (but less than six months) if the veteran is certified as being in receipt of unemployment compensation under State or Federal law for not less than four weeks (but less than six months) during the one year period ending on the hiring date.
- o An unemployed veteran or disconnected youth hired in 2009 or 2010.

The bill would modify the reference to the "United States Employment Service, in consultation with the Internal Revenue Service" to read, "The Employment Development Department (EDD), in consultation with the Franchise Tax Board (FTB)."

The bill would not allow a credit for second year wages paid to long term family assistance employees. Further, the bill states that the rules provided in the IRC for either agricultural labor or railway labor or certain Individuals not meeting minimum employment periods would not apply.

The bill states that the qualified employer would be allowed the California WOTC in the taxable year in which the employer receives certification or in the taxable year in which the qualified employer paid or incurred the qualified first year wages.

The EDD would be required to issue certification of qualified individuals, consistent with the requirements of the federal WOTC, as modified by this bill. Absent such certification, no credit would be allowed.

The bill would allow the California WOTC to be carried over for up to 10 years until the credit is exhausted.

Deductions otherwise allowed for qualified wages paid or incurred would be required to be reduced by the amount of the California WOTC allowed.

The Department of Finance (DOF) would be required to estimate the total dollar amount of credits claimed under this section for each tax year from 2021-2022 fiscal year to 2025-2026 fiscal year.

The FTB would be required to provide an annual report to the Joint Legislative Budget Committee, no later than March 1, which includes the following:

- The total dollar amount of the credit claimed under this section with respect to the relevant fiscal year.
- A comparison of the total dollar amount of credits claimed to the DOF's estimate with respect to that same fiscal year.

- The number of tax returns claiming the credit.
- The number of qualified individuals represented on tax returns claiming the credit.

The credit would be repealed by its own terms on December 1, 2025.

This bill, in compliance with RTC section 41, would specify the following:

- The purpose of the tax expenditure would be to encourage employers to retain and hire individuals from identified targeted groups who face systemic employment barriers.
- EDD would be required to prepare a written report annually on the following:
  - Number of employers, based on employer IDs, who filed for certification,
  - Number and percentage of employees that were granted certification,
  - The distribution of newly hired employees over the eight eligible targeted groups, and
  - The distribution of employers and employees based on industry sectors.
- EDD would also be required on or before October 1, 2021, and thereafter annually to post on its internet website, the annual written report and also deliver a letter to the Secretary of the Senate and the Chief Clerk of the Assembly within four calendar days indicating that the report has been posted.

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, 2021, and before January 1, 2025.

Federal Law

The WOTC is a federal income tax credit available to employers who hire and retain veterans and individuals from targeted groups with significant barriers to employment. There is no limit on the number of individuals an employer can hire to qualify to claim the WOTC.

The amount of the WOTC employers may claim varies based on the target group of the individual hired, the wages paid to that individual in the first year of employment, and the number of hours that individual worked. There is a maximum amount of WOTC that can be earned for each targeted group.

For the long-term Temporary Assistance for Needy Families (TANF) target group only, the WOTC is available to employers who hire members of this group for up to a two-year period.

- In the first year, the employer may claim a tax credit equal to 40 percent of the first-year wages, up to the maximum tax credit, if the individual works at least 400 hours.
- In the second year, the employer may claim a tax credit equal to 50 percent of the second-year wages, up to the maximum tax credit, if the individual works at least 400 hours.

For all other target groups, the WOTC is available to employers who hire members of these groups, based on the individual's hours worked and wages earned in the first year.

- If the individual works at least 120 hours, the employer may claim a tax credit equal to 25 percent of the individual's first year wages, up to the maximum tax credit.
- If the individual works at least 400 hours, the employer may claim a tax credit equal to 40 percent of the individual's first year wages, up to the maximum tax credit.

The Consolidated Appropriations Act (CAA), 2021 (PL 116-260) extended the federal WOTC until December 31, 2025, and applies to individuals who begin work for employers after December 31, 2020.

State Law

For taxable years beginning on or after January 1, 2014, and before January 1, 2021, 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. In order to claim the state credit, the qualified taxpayer must receive a tentative credit reservation from the FTB for that qualified full-time employee.

Implementation Considerations

Implementing this bill would require some changes to existing tax forms and instructions and information systems, which could be accomplished during the normal annual update.

This bill would require the department to provide a report on the utilization of this credit by March 1, 2022. The department would not have that specific data until after July 2023. The author may wish to amend the bill to change the due date of the report to allow the department time to collect the necessary data.

Technical Considerations

None noted.

Policy Considerations

The report requires the total dollar amount of the credits claimed to be provided with respect to the relevant fiscal year (Sections 17053.71 and 23672(g)(2)(A)). Personal income tax returns may be filed, with extension, until October 15 and are filed on a calendar year basis. Corporate returns may be filed even later, depending on when the taxpayer's fiscal year ends. The department also requires time to process returns. The author may want to use "taxable year" instead of "fiscal year" to ensure that the report contains the necessary and most up to date total dollar amount of credit information.

In addition, the author may wish to add, similar to the deduction, language that reduces by the amount of WOTC that can be claimed should the qualified wages be used in the calculation of another wage credit.

LEGISLATIVE HISTORY

AB 1726 (Arambula and Cerantes, 2019/20) and AB 916 (Quirk-Silva & Arambula, 2017/2018) would have created a tax credit for certain employers that hire employees who are members of a targeted group. AB 1726 did not pass out of the Assembly by the constitutional deadline, and AB 916 did not pass out of the Senate Committee on Appropriations.

PROGRAM BACKGROUND

Not applicable.

FISCAL IMPACT

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

ECONOMIC IMPACT

Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of SB 553 as Amended April 15, 2021
Assumed Enactment after June 30, 2021

($ in Millions)

Fiscal Year	Revenue
2021-2022	-$110.0
2022-2023	-$110.0
2023-2024	-$120.0

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

This estimate is based on a proration of the Joint Committee on Taxation (JCT) federal estimate for the WOTC. In December 2020, the JCT estimated the federal loss would be $2.1 billion in the 2021 taxable year. California's taxpayers account for approximately 8 percent, or $160 million, of the total WOTC earned. An adjustment of approximately $75 million was made to account for federal and state differences in the calculation of the credit, as well as for taxpayers who would take the federal WOTC but not the California WOTC. This would result in credits generated of approximately $85 million in the 2021 taxable year.

As set forth in the bill, wages that would otherwise be allowed as a deduction under current law would be reduced by the amount of credit allowed. It is estimated that qualified taxpayers would be able to deduct approximately $85 million of qualified expenses in the 2021 taxable year. Applying an average tax rate of 7 percent, results in an offsetting revenue gain of $6 million. This would result in an estimated net revenue loss of approximately $80 million in the 2021 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

To be determined.

ARGUMENTS

To be determined.

LEGISLATIVE CONTACT

FTBLegislativ eServ ices@ftb.ca.gov