

**DESCRIPTION OF PRESENT LAW AND
PROPOSALS RELATING TO THE
WORK OPPORTUNITY TAX CREDIT**

Scheduled for a Public Hearing

Before the

SUBCOMMITTEE ON OVERSIGHT

of the

HOUSE COMMITTEE ON WAYS AND MEANS

on July 1, 1999

Prepared by the Staff

of the

JOINT COMMITTEE ON TAXATION



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INTRODUCTION

The Subcommittee on Oversight of the House Committee on Ways and Means has scheduled a public hearing on July 1, 1999, to review the work opportunity tax credit, which is scheduled to expire after June 30, 1999.

This document,¹ prepared by the staff of the Joint Committee on Taxation, provides a description of present law and legislative proposals relating to the work opportunity tax credit.

Part I of this document is a summary of present law. Part II describes the present-law rules for the work opportunity tax credit. Part III describes the Administration's and the House legislative proposals (106th Congress) relating to the work opportunity tax credit.

¹ This document may be cited as follows: Joint Committee on Taxation, *Description of Present Law and Proposals Relating to the Work Opportunity Tax Credit* (JCX-41-99), June 29, 1999.

I. SUMMARY

In general

The work opportunity tax credit ("WOTC"), which is scheduled to expire after June 30, 1999, is available on an elective basis for employers hiring individuals from one or more of eight targeted groups. The credit equals 40 percent (25 percent for employment of 400 hours or less) of qualified wages. Generally, qualified wages are wages attributable to service rendered by a member of a targeted group during the one-year period beginning with the day the individual began work for the employer.

The maximum credit per employee is \$2,400 (40 percent of the first \$6,000 of qualified first-year wages). With respect to qualified summer youth employees, the maximum credit is \$1,200 (40 percent of the first \$3,000 of qualified first-year wages).

The employer's deduction for wages is reduced by the amount of the credit.

Targeted groups eligible for the credit

The eight targeted groups are: (1) families eligible to receive benefits under the Temporary Assistance for Needy Families ("TANF") Program; (2) qualified veterans; (3) qualified ex-felons; (4) high-risk youths; (5) vocational rehabilitation referrals; (6) qualified summer youth employees; (7) families receiving food stamps; and (8) persons receiving certain Supplemental Security Income ("SSI") benefits.

Minimum employment period

No credit is allowed for wages paid to employees who work less than 120 hours in the first year of employment.

Expiration date

Under present law, the credit is scheduled to expire for wages paid or incurred to an otherwise qualified individual who begins work for an employer on or after July 1, 1999.

II. PRESENT LAW

In general

The work opportunity tax credit (sec.51) is available on an elective basis for employers hiring individuals from one or more of eight targeted groups. The credit generally is equal to 40 percent (25 percent for employment of 400 hours or less) of qualified wages. Generally, qualified wages consist of wages attributable to service rendered by a member of a targeted group during the one-year period beginning with the day the individual begins work for the employer.

Generally, no more than \$6,000 of wages during the first year of employment is permitted to be taken into account with respect to any individual. Thus, the maximum credit per individual is \$2,400. With respect to qualified summer youth employees, the maximum credit is \$1,200 (40 percent of up to \$3,000 of qualified first-year wages).

The deduction for wages is reduced by the amount of the credit.

Targeted groups eligible for the credit

- (1) Families receiving benefits under Title IV-A of the Social Security Act (The Temporary Assistance for Needy Families Program ("TANF"))

An eligible recipient is an individual certified by the designated local employment agency as being a member of a family eligible to receive benefits under (Title IV-A of the Social Security Act) for a period of at least nine months (whether or not consecutive), during the 18-month period ending on the hiring date. For these purposes, members of the family are defined to include only those individuals taken into account for purposes of determining eligibility for the Title IV-A program.

- (2) Qualified veteran

A qualified veteran is a veteran who is a member of a family certified as receiving assistance under a food stamp program under the Food Stamp Act of 1977 for a period of at least three months part of which is during the 12-month period ending on the hiring date. For these purposes, members of a family are defined to include only those individuals taken into account for purposes of determining eligibility for a food stamp program under the Food Stamp Act of 1977.

A veteran is an individual who has served on active duty (other than for training) in the Armed Forces for more than 180 days or who has been discharged or released from active duty in the Armed Forces for a service-connected disability. However, any individual who has served for a period of more than 90 days during which the individual was on active duty (other than for training) is not an eligible employee if any of this active duty occurred during the 60-day period

ending on the date the individual was hired by the employer. This latter rule is intended to prevent employers who hire current members of the armed services (or those departed from service within the last 60 days) from receiving the credit.

(3) Qualified ex-felon

A qualified ex-felon is an individual certified as: (1) having been convicted of a felony under any State or Federal law; (2) being a member of a family that had an income during the six months before the earlier of the date of determination or the hiring date which on an annual basis is 70 percent or less of the Bureau of Labor Statistics lower living standard; and (3) having a hiring date within one year of release from prison or date of conviction.

(4) High-risk youth

A high-risk youth is an individual certified as being at least 18 but not yet 25 on the hiring date and as having a principal place of abode within an empowerment zone or enterprise community (as defined under Subchapter U of the Internal Revenue Code). Qualified wages will not include wages paid or incurred for services performed after the individual moves outside an empowerment zone or enterprise community.

(5) Vocational rehabilitation referral

Vocational rehabilitation referrals are those individuals who have a physical or mental disability that constitutes a substantial handicap to employment and who have been referred to the employer while receiving, or after completing, vocational rehabilitation services under an individualized, written rehabilitation plan under a State plan approved under the Rehabilitation Act of 1973 or under a rehabilitation plan for veterans carried out under Chapter 31 of Title 38, U.S. Code. Certification will be provided by the designated local employment agency upon assurances from the vocational rehabilitation agency that the employee has met the above conditions.

(6) Qualified summer youth employee

Qualified summer youth employees are individuals: (1) who perform services during any 90-day period between May 1 and September 15; (2) who are certified by the designated local agency as being 16 or 17 years of age on the hiring date or if later, May 1st of the calendar year involved; (3) who have not been an employee of that employer before; and (4) who are certified by the designated local agency as having a principal place of abode within an empowerment zone or enterprise community (as defined under Subchapter U of the Internal Revenue Code). As with high-risk youths, no credit is available on wages paid or incurred for service performed after the qualified summer youth moves outside of an empowerment zone or enterprise community. If, after the end of the 90-day period, the employer continues to employ a youth who was certified

during the 90-day period as a member of another targeted group, the limit on qualified first-year wages will take into account wages paid to the youth while a qualified summer youth employee.

(7) Families receiving food stamps

An eligible recipient is an individual aged 18 but not yet 25 on the hiring date certified by a designated local employment agency as being a member of a family receiving assistance under a food stamp program under the Food Stamp Act of 1977 for a period of at least six months ending on the hiring date. In the case of families that cease to be eligible for food stamps under section 6(o) of the Food Stamp Act of 1977, the six-month requirement is replaced with a requirement that the family has been receiving food stamps for at least three of the five months ending on the date of hire. For these purposes, members of the family are defined to include only those individuals taken into account for purposes of determining eligibility for a food stamp program under the Food Stamp Act of 1977.

(8) Qualified supplemental security income (“SSI”) recipients

An eligible recipient is an individual certified by a designated local agency as receiving supplemental security income (“SSI”) benefits under Title XVI of the Social Security Act (including supplemental security income benefits of the type described in section 1616 of such Act or section 212 of Public Law 93-66) for any month ending within the 60-day period ending on the hiring date.

Certification of targeted groups

In general, an individual is treated as a member of a targeted group if: (1) on or before the individual begins work for an employer, the employer receives a certification from a designated local agency that such individual is a member of a targeted group; or (2) on or before the individual is offered employment with the employer, a pre-screening notice is completed by the employer and not later than the 21st day after the individual begins work for the employer, the employer submits such notice to the designated local agency as part of a written request for certification from such agency.

If an individual is certified by the designated local agency as a member of a targeted group and such certification is incorrect because it was based on false information provided by such individual, the certification will be revoked and wages paid to that individual after the date on which notice of such revocation is received by the employer are not qualified wages for purposes of the credit.

If a designated local agency denies a request for certification, the agency should provide the individual with a written explanation of the reasons for the denial.

Minimum employment period

No credit is allowed for wages paid unless the eligible individual is employed by the employer for at least 120 hours in the first year of employment.

Definition of wages

In general, wages eligible for the credit are defined by reference to the definition of wages under the Federal Unemployment Tax Act (FUTA) in section 3306(b) of the Code, except that the dollar limits of that section do not apply. Because wages paid to certain agricultural and railroad employees are not FUTA wages, special rules are provided for these wages.

Wages may be taken into account for purposes of the credit only if more than one-half of the wages paid during the taxable year to an employee are for services in the employer's trade or business. The test as to whether more than one-half of an employee's wages are for services in a trade or business is applied to each separate employer without treating related employers as a single employer.

Other rules

The amount of the credit (together with the other nonrefundable credits) may be claimed only to the extent the regular tax exceeds the tentative minimum tax. In addition, the amount of the credit (together with the other nonrefundable credits) may not exceed the sum of the first \$25,000 of the taxpayer's regular tax and 75 percent of the remainder of that tax. Any excess credit may be carried back one year and forward 20 years.

All employees of all corporations that are members of a controlled group of corporations are to be treated as if they were employees of the same corporation for purposes of determining the years of employment of any employee and wages for any employee up to \$6,000. Generally, under the controlled group rules, the credit allowed the group is the same as if the group were a single company. A comparable rule is provided in the case of partnerships, sole proprietorships, and other trades or businesses (whether or not incorporated) that are under common control, so that all employees of such organizations generally are to be treated as if they were employed by a single person. The amount of work opportunity tax credit allowable to each member of the controlled group is its proportionate share of the wages giving rise to the credit.

No credit is available for the hiring of certain related individuals (primarily dependents or owners of the taxpayer). The credit is also not available for wages paid to an individual who was employed by the employer at any time during which the individual was not a certified member of a targeted group.

Expiration date

The credit is effective for wages paid to, or incurred with respect to, a qualified individual who begins work for an employer after September 30, 1996, and before July 1, 1999.

III. ADMINISTRATION AND HOUSE LEGISLATIVE PROPOSALS

1. Administration Proposal

The Administration proposal would extend the work opportunity tax credit for one year (through June 30, 2000). The proposal would also clarify the coordination of the WOTC and the welfare-to-work tax credit with respect to an individual whose first year of employment does not coincide with the employer's taxable year.

2. H.R. 81 (Mr. Bilirakis)

H.R. 81 would add a new targeted category of displaced homemakers to the credit. A displaced homemaker is defined as an individual who: (1) has not worked in the labor force for at least five years but rather performed unpaid services in the home for family members; and (2) has been dependent on public assistance or the income of another family member but is no longer supported by that income or is currently receiving public assistance on account of dependent children in the home. The bill would also repeal the expiration of the work opportunity tax credit for purposes of the displaced homemaker targeted group.

3. H.R. 585 (Mr. English)

H.R. 585 would allow the work opportunity tax credit to be claimed against either the taxpayer's regular tax or alternative minimum tax ("AMT") liability (i.e., repealing the present-law limitations on the credit against the AMT).

4. H.R. 671 (Mr. Cardin, Mr. Stark, Mr. Matsui, Mr. Coyne, Mr. Jefferson)

In the context of a package of proposals to help foster children make the transition to independent adults, H.R. 671 would add a new category of qualified foster care recipients to the credit. A qualified former foster care recipient is defined as an individual certified by a local designated agency as: (1) being at least age 18 but not 25 on the hiring date; and (2) on the day before attaining age 18, either being a recipient of foster care maintenance payments under a State plan approved under Title IV-E of the Social Security Act or in foster care under the responsibility of a State.

5. H.R. 815 (Mr. Watts, Mr. Weller, Mr. Hulshof and others)

In the context of a package of proposals to designate renewal communities and provide tax incentives thereto, H.R. 815 would expand the high-risk youth and qualified summer youth employee categories to include qualifying individuals with a principal place of abode in renewal communities. The maximum credit for these two categories also would be modified to 15

percent of the first \$10,000 of qualified first-year wages and 30 percent of the first \$10,000 of qualified second-year wages.

6. H.R. 998 (Mr. Hayes)

H.R. 998 would add a new category of rural area residents to the credit. A rural area resident is defined as any employee of an employer with respect to any period if: (1) substantially all the services performed in such period by the employee for the employer are performed within an area determined by the Secretary of Agriculture to be a rural area; and (2) the principal place of abode of the employee while performing such services is within such area.

7. H.R. 1084 (Ms. Dunn, Mr. Weller and others)

In the context of a larger tax relief package, H.R. 1084 would permanently extend the work opportunity tax credit.

8. H.R. 2101 (Mr. Houghton, Mr. Rangel, Mr. Weller, Mr. Lewis of Georgia, Mrs. Johnson of Connecticut, Mr. Matsui, Mr. Ramsted, Mr. Hayworth, Mr. Lewis of Kentucky, Mr. Watkins, Mr. Levin, Mr. McNulty, Mr. Cardin, Mr. Neal of Massachusetts, Ms. Dunn, Mr. English, Mr. Foley, Mr. McInnis, Mrs. Thurman, Mr. Jefferson, Mr. Coyne, Mr. Becerra, Mr. Stark, Mr. Nussle, and others)

H.R. 2101 would permanently extend the work opportunity tax credit. It would also consolidate the work opportunity tax credit with the welfare-to-work tax credit ("WWTC") by making three principal changes to the WOTC. First, the definition of eligible wages for WOTC (i.e. cash wages as defined for Federal Unemployment Tax purposes) would be expanded to include the broader wage base allowed under the WWTC. Thus eligible wages under the consolidated credit would include cash wages paid to an employee plus amounts paid by the employer for the following: (1) educational assistance excludable under a section 127 program (or that would be excludable but for the expiration of sec. 127); (2) health plan coverage for the employee, but not more than the applicable premium defined under section 4980B(f)(4); and (3) dependent care assistance excludable under section 129. Second, the welfare-to-work targeted category would be added to the other targeted categories in the WOTC at a credit rate of 40 percent of both first-year wages and second-year wages. Third, the wage base for purposes of the welfare-to-work targeted category alone, would be expanded to \$10,000 of first-year wages and \$10,000 of second-year wages. The present-law WOTC wage base (\$6,000 of first-year wages) would be unchanged for purposes of the other targeted groups. Finally, H.R. 2101 would extend the new consolidated credit to eligible tax-exempt employers by allowing the credit against Social Security tax liability for them.