LEGISLATIVE FISCAL OFFICE
Fiscal Note

Louisiana Legislative Fiscal Office Fiscal Notes

Fiscal Note On: **HB 523** HLS 19RS 754
Bill Text Version: **ORIGINAL**
Opp. Chamb. Action:
Proposed Amd.:
Sub. Bill For.:

Date: April 22, 2019 7:05 PM **Author:** IVEY
Dept./Agy.: Revenue
Subject: Phase Out Corporate Franchise Tax, Repeal Certain Credits **Analyst:** Greg Albrecht

TAX OR -$34,000,000 GF RV See Note

Phases-out the corporate franchise tax and repeals certain income and corporate franchise tax credits

Proposed law phases out the corporate franchise tax evenly over a 4-year period, beginning with taxable years beginning on and after January 1, 2020.
Present law provides a tax credit to certain industries for local property tax paid on inventory, with limited refundability.
Proposed law reduces the credit to 50% of property taxes paid on or after January 1, 2018, and makes the credit nonrefundable for all claimants, with a five-year carry-forward.
Proposed law repeals various other tax credits.
Effective for franchise tax and income tax periods beginning on or after January 1, 2020.

Contingent upon adoption of a constitutional amendment contained in an unspecified instrument of this session.

EXPENDITURES	2019-20	2020-21	2021-22	2022-23	2023-24	5 -YEAR TOTAL
State Gen. Fd.	INCREASE	INCREASE	INCREASE	INCREASE	INCREASE	
Agy. Self-Gen.	$0	$0	$0	$0	$0	**$0**
Ded./Other	$0	$0	$0	$0	$0	**$0**
Federal Funds	$0	$0	$0	$0	$0	**$0**
Local Funds	$0	$0	$0	$0	$0	**$0**
Annual Total						

REVENUES	2019-20	2020-21	2021-22	2022-23	2023-24	5 -YEAR TOTAL
State Gen. Fd.	($34,000,000)	($89,000,000)	($75,000,000)	($125,000,000)	($150,000,000)	**($473,000,000)**
Agy. Self-Gen.	$0	$0	$0	$0	$0	**$0**
Ded./Other	$0	$0	$0	$0	$0	**$0**
Federal Funds	$0	$0	$0	$0	$0	**$0**
Local Funds	$0	$0	$0	$0	$0	**$0**
Annual Total	**($34,000,000)**	**($89,000,000)**	**($75,000,000)**	**($125,000,000)**	**($150,000,000)**	**($473,000,000)**

EXPENDITURE EXPLANATION

Tax system changes will have to be made each year to provide for the changing tax liability calculation over the life of the phase-out. These changes are typically estimated as several thousands of dollars of staff time for design, modification, and testing (estimated at $26,000 per year in this case). In addition, a phase-out of the tax will likely result in some confusion among taxpayers regarding their tax liability for particular years, amended returns, and prior year overpayments. Additional costs will be incurred communicating with and advising taxpayers as the phase-out progresses.

REVENUE EXPLANATION

Rough estimates of the annual state tax revenue losses of the bill are $34 million in FY20, $89 million lost in FY21, $75 million lost in FY22, $146 million lost in FY23, and $221 million lost in FY23. By the third or fourth year the credit repeals in the bill would likely be providing an accumulating net tax gain of an amount to be materially offsetting the the franchise tax revenue losses (gross losses in FY23 & FY24 moderated in table above). However, by FY25, the franchise tax would be fully phased out, and the credit modifications and repeals fully operative, but the net state loss would still likely be near $200 million per year.

Franchise Tax Phase-out: The base of the estimated revenue phase-out was established by the Dept. of Revenue as the franchise tax liabilities after nonrefundable credits for tax year 2016, the most current complete filing year, inclusive of the extension of the tax to LLCs. This base is $377 million. The bill's 4-year even phase-out generates a schedule of liability reductions starting at 25% or $94.3 million in the first year, accumulating by that amount each year for four years until the entire $377 million liability reduction is effective for tax year 2024. Liability reductions are first realized in FY20 because the franchise tax is due at the beginning of the tax year, and the bill begins the phase-out with tax year 2020.

This simple phase-out is complicated by the fact that in any particular fiscal year returns are filed for a number of prior tax years. Past filing patterns suggest that within a fiscal year, 45% of franchise tax returns apply to the immediate tax year, 50% to the preceding tax year, and 5% from earlier tax years. Incorporating these factors into the phase-out schedule, results in a first fiscal year revenue reduction of $42.4M ($377M x 25% x 45%). The second year reduction will include a 50% filing factor applied to the first year's 25% tax reduction plus the second year's 50% tax reduction and a 45% filing factor, resulting in a $132.1M revenue reduction. The third year reduction will include a 5% filing factor applied to the first year's 25% reduction plus a 50% filing factor applied to the second year's 50% tax reduction plus the third year's 75% tax reduction with a 45% filing factor, resulting in a $226.4M revenue reduction. This pattern accumulates the tax year liability reductions realized in fiscal years over a six year period before the full amount of corporate franchise tax revenue is eliminated in FY25.

Senate — Dual Referral Rules

- [ ] 13.5.1 >= $100,000 Annual Fiscal Cost {S & H}
- [x] 13.5.2 >= $500,000 Annual Tax or Fee Change {S & H}

House

- [ ] 6.8(F)(1) >= $100,000 SGF Fiscal Cost {H & S}
- [ ] 6.8(G) >= $500,000 Tax or Fee Increase or a Net Fee Decrease {S}

John D. Carpenter
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CONTINUED EXPLANATION from page one:

Continued Revenue Explanation

Franchise Tax Phase-out continued:
Actual revenue reductions are further complicated by the carry-forward of overpayments from prior years, which are still due to the taxpayer even if the tax is phased out. For the base tax year of 2016, the franchise tax credit carry-forward was some $149 million. Taxpayers will claim these refunds in the years of the phase-out, increasing the annual revenue reduction estimates above.

In addition, refundable tax credits and rebate payments charged against the franchise tax will continue to be refunded and paid as they will be shifted to the income tax. This, in combination with claims of refund carry-forwards, and the normal variability of the tax, means that actual tax receipt changes in any particular fiscal year can differ materially from those estimated above.

Inventory Tax Credit Modifications: The Dept. of Revenue assessed tax returns claiming the inventory credit, and estimates that the modifications proposed by this bill will reduce the amount of tax credit that could be realized by taxpayers each year by some $103 million. Past filing patterns suggest that within a fiscal year, 11% of income and franchise tax returns as a group apply to the immediate tax year, 84% to the preceding tax year, and 5% from earlier tax years. Incorporating these factors, results in a first fiscal year revenue increase of $11.3M, a second year increase of $97.9M, and by the third year the full $103M.

Repeal of Various Other Credits
The bill repeals various tax credits effective for tax periods beginning January 1, 2020. A number of these credits are small and erratic in utilization, the repeal of which would have little material effect on net state revenue collections. A few of the credits are large and would make up the large majority of affected revenue. These large credits include the historic preservation credit, the retention & modernization credit, the angel investor credit, the musical & theatrical productions credit, and the citizens insurance assessment credit. As a group, these credits reduce state tax collections in excess of $100 million per year. However, a repeal of them does not generate large net tax collections initially. R.S. 47:1675 provides that carry-forwards of unused credits shall continue to be available to taxpayers. The Dept. estimates that in the FY20 - FY24 period, only about $5 million - $7 million of repeal effect would increase net tax collections (from the repeal of the citizens assessment credit, the small-town medical professionals credits, and the alternative fuel vehicle conversion credit). The large bulk of effect from repeal would come from the historic preservation credit, which has a five-year carry-forward (for example $101 million of historic preservation credit in FY18). Thus, projects earning credits in 2019 would be able to use those credits as far in the future as the 2024 return, filed in FY25. Some slow accumulation of net tax collections would occur over the next several years as participants completed their respective credit programs with no new participants entering those programs.

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