LEGISLATIVE FISCAL OFFICE
Fiscal Note

Fiscal Note On: **HB 828** HLS 15RS 1665
Bill Text Version: **REENGROSSED**
Opp. Chamb. Action:
Proposed Amd.:
Sub. Bill For.:

Date: May 29, 2015 1:05 PM
Author: HENRY
Dept./Agy.: Revnue
Subject: Phase Out Corporate Franchise Tax
Analyst: Greg Albrecht

TAX/CORP FRANCHISE
Phases out corporation franchise tax

RE -$36,500,000 GF RV See Note

Current law levies a tax on taxable capital of 0.15% of the first $300,000 and 0.3% above $300,000.

Proposed law phases out the franchise tax evenly over five years (20% per year), starting with taxable years beginning January 1, 2016 and before January 1, 2017.

Effective if HB 629 of the 2015 session is enacted and becomes effective. HB 629 reduces most corporate income and franchise tax credits by 20%.

EXPENDITURES	2015-16	2016-17	2017-18	2018-19	2019-20	5 -YEAR TOTAL
State Gen. Fd.	$0	$0	$0	$0	$0	**$0**
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	**$0**	**$0**	**$0**	**$0**	**$0**	**$0**

REVENUES	2015-16	2016-17	2017-18	2018-19	2019-20	5 -YEAR TOTAL
State Gen. Fd.	($36,500,000)	($109,500,000)	($182,500,000)	($255,500,000)	($328,500,000)	**($912,500,000)**
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	**($36,500,000)**	**($109,500,000)**	**($182,500,000)**	**($255,500,000)**	**($328,500,000)**	**($912,500,000)**

EXPENDITURE EXPLANATION

The Department of Revenue will incur costs involved in modifying its systems dealing with the corporate franchise tax. Taxpayer education and compliance support expenses may also be incurred. These costs should be minor and one-time in nature.

REVENUE EXPLANATION

There is considerable uncertainty as to how much revenue would be lost each year as a result of a phase out of the corporate franchise tax. Using FY14 as a model, the reported amount of franchise tax collections in FY14 net of amnesty, nonrefundable credits, and refundable credits was some $160 million. That may be taken as an approximation of the minimum amount of revenue loss on a full tax basis that can be expected. Accumulating 20% increments of tax reduction may give an approximation of the minimum tax loss each year ($32M in year 1, $64M yr2, $96M yr3, $128M yr4, and $160M yr5). However, it is the gross tax before any credits that is being phased out. Again, using FY14 as a model, the total amount of franchise tax due on returns filed that year was $460 million. Of that total, $65 million was associated with the tax amnesty program, leaving $395M of base collections. Approximately $30 million per year of nonrefundable credits has been taken against the franchise tax in recent years. These credits are unlikely to migrate to the income tax since they tend to be claimed against franchise tax because little or no income tax liability exists on these returns. Refundable credits claimed against franchise tax will migrate to the income tax, where they are not now expected. Thus, $365 million is the gross tax amount that the bill phases out evenly over a five year period. In addition, roughly half the returns with positive franchise tax amounts filed in a fiscal year relate to the immediately preceding tax period, and half to the tax period two years preceding.

All these considerations result in the following pattern of revenue loss: in FY16, $109.5M = 1/2 of $365M x 20%; in FY17, $109.5 = 1/2 of $365M x 20% + 1/2 of $365M x 40%; in FY18, $182.5 = 1/2 of $365M x 40% + 1/2 of $365M x 60%; in FY19, $255.5 = 1/2 of $365M x 60% + 1/2 of $365M x 80%; and, in FY20, $328.5 = 1/2 of $365M x 80% + 1/2 of $365M x 100%. By FY21, 100% of the franchise tax will be eliminated. There will likely be more than two preceding tax periods in each fiscal year's returns, but this trailing or residual effect is ignored for simplicity. In addition, only the FY14 year is utilized for an estimate as recent years have experienced dramatic national expansion and recession, borrowed capital phase-out, and tax amnesties.

Another issue involves refund carryforwards, where taxpayers are due refunds but choose to apply them to future tax liabilities. In FY14 there were $409M of refund carryforwards associated with the combined corporate income and franchise tax. It is not known at this time how much is specifically attributable to franchise tax; but 25% or more is possible. Presumably, these refunds will have to be paid at some time during the phase out period.

Senate — Dual Referral Rules — House

- [ ] 13.5.1 >= $100,000 Annual Fiscal Cost {S&H}
- [x] 13.5.2 >= $500,000 Annual Tax or Fee Change {S&H}
- [ ] 6.8(F)(1) >= $100,000 SGF Fiscal Cost {H & S}
- [x] 6.8(F)(2) >= $500,000 Rev. Red. to State {H & S}
- [ ] 6.8(G) >= $500,000 Tax or Fee Increase or a Net Fee Decrease {S}

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