COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 0446-04
Bill No.: Perfected HCS for HB 76
Subject: Corporations; Revenue Dept; Taxation and Revenue - General
Type: Original
Date: March 1, 2011

Bill Summary: Would phase out the corporate franchise tax over five years and limit a corporation's franchise tax to the prior year amount.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2012	FY 2013	FY 2014
General Revenue *	$0	($16,554,054 to Unknown)	($35,000,000 to Unknown)
Total Estimated Net Effect on General Revenue Fund *	**$0**	**($16,554,054 to Unknown)**	**($35,000,000 to Unknown)**

* Including unknown estimated future revenue foregone.

ESTIMATED NET EFFECT ON OTHER STATE FUNDS			
FUND AFFECTED	FY 2012	FY 2013	FY 2014
Total Estimated Net Effect on Other State Funds	**$0**	**$0**	**$0**

Numbers within parentheses: ( ) indicate costs or losses.
This fiscal note contains 8 pages.

ESTIMATED NET EFFECT ON FEDERAL FUNDS			
FUND AFFECTED	FY 2012	FY 2013	FY 2014
Total Estimated Net Effect on All Federal Funds	**$0**	**$0**	**$0**

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)			
FUND AFFECTED	FY 2012	FY 2013	FY 2014
Total Estimated Net Effect on FTE	**0**	**0**	**0**

☒ Estimated Total Net Effect on All funds expected to exceed $100,000 savings or (cost).

☐ Estimated Net Effect on General Revenue Fund expected to exceed $100,000 (cost).

ESTIMATED NET EFFECT ON LOCAL FUNDS			
FUND AFFECTED	FY 2012	FY 2013	FY 2014
Local Government	**$0**	**$0**	**$0**

FISCAL ANALYSIS

ASSUMPTION

Officials from the **Office of Administration, Division of Budget and Planning** (BAP) assume this proposal would not result in additional savings or costs to their organization.

This proposal, as amended, would phase out franchise taxes over five years, starting with tax years beginning on or after 1/1/12, which would impact franchise tax payments beginning in FY12; would cap franchise tax liability at the tax year 2010 levels, and would provide a tax credit for financial institutions that are LLCs or LLPs.

BAP officials defer to the Department of Revenue for estimates of reduced general and total state revenues.

Officials from the **Department of Revenue** (DOR) assume this proposal would change the corporate franchise and bank franchise tax rates and would eventually phase out the tax, which would create a negative impact to total state revenue.

For all years beginning on or after January 1, 2011, but before December 31, 2015, a corporation's franchise tax liability under this chapter would not exceed the amount of annual franchise tax liability for the taxable year ending on or before December 31, 2010.

If the corporation had no franchise tax liability for the year ending on or before December 31, 2010, because such corporation was not in existence or doing business in Missouri, the franchise tax for the first taxable year in which such corporation exists would be determined by applying the applicable rate of tax to the corporation's outstanding shares and surplus if the outstanding shares and surplus exceed ten million dollars; but in no case would such corporation's tax liability for any subsequent year exceed the amount of franchise tax for the first full year such corporation was in existence or doing business in Missouri.

Between January 1, 2010 and January 1, 2012, the annual franchise tax would be 1/30th of one percent of the taxable entity's outstanding shares and surplus, if they exceed $10.0 million. For 2012 the rate would be 1/37th of one percent, for 2013 the rate would be 1/50th of one percent, for 2014 the rate would be 1/75nd of one percent, for 2015 the rate would be 1/150th of one percent, and for tax years beginning on or after January 01, 2016, no franchise tax would be imposed.

ASSUMPTION (continued)

Assets levels reported for corporate franchise tax filers that have assets greater than $10 million have increased at a rate of 6.23% per year since 2002. The following table reflects the anticipated reduction in corporation franchise tax, if asset levels continue to increase as the tax is phased out.

Corporate Franchise

Year	Assets	Rate	Tax	Reduction in tax
2009	$249,077,742,304	0.000333	$82,942,888	$0
2012	$298,590,829,277	0.000266	$79,425,161	$3,517,728
2013	$317,193,037,941	0.000200	$63,438,608	$19,504,281
2014	$336,954,164,205	0.000133	$44,814,904	$38,127,984
2015	$357,946,408,635	0.000067	$23,982,409	$58,960,479
2016	NA	0.000000	$0	$82,942,888

Oversight notes that franchise tax collections fluctuate from year to year, and assumes that this proposal could result in a reduction of revenues in the future if the DOR estimate of future taxable capital and surplus is realized. For fiscal note purposes only, Oversight will indicate an unknown revenue reduction for the General Revenue Fund for the foregone potential future revenue due to increased amounts of taxable capital and surplus.

Bank Franchise

Fiscal year 2010 bank franchise tax collections were $5.7 million. A reduction similar to the corporate franchise tax would also result to bank franchise tax collections.

DOR officials stated that the Department and the Office of Administration, Information Technology Services Division (ITSD-DOR) would need to make programming changes to the corporation income tax processing systems (COINS and CAFÉ), Corp E-file System and the Financial Institutions Tax System. DOR officials estimated the IT portion of the fiscal impact at $40,068, based on 1,512 hours of programming time.

ASSUMPTION (continued)

Oversight assumes that ITSD-DOR is provided with core funding to handle a certain amount of activity each year, and assumes ITSD-DOR could absorb the costs related to this proposal. If multiple bills pass which require additional staffing and duties at substantial costs, ITSD-DOR could request funding through the appropriation process.

Officials from the **University of Missouri, Economic and Policy Analysis Research Center** (EPARC) assume that if enacted, this legislation would gradually phase-out the corporate franchise tax over a five year period.

For the tax year 2011, the rate would remain at one-thirtieth of one percent and the threshold amount would remain at $10 million dollars. For 2012, the rate would be reduced to one thirty-seventh of one percent. For the tax year 2013, the rate would be reduced to one fiftieth of one percent. For the tax year 2014, the rate would be reduced to one seventy-fifth of one percent. For the tax year 2015, the rate would decrease to one hundred-fiftieth of one percent. Effective January 1, 2016, no corporate franchise tax would be imposed.

The following estimates were generated using corporate tax data from 2008. The table reports the potential total franchise tax for corporations with assets greater than $10 million in Missouri for the years 2011 through 2016 if this proposal was implemented.

Year	Franchise Tax Rate	Franchise Tax Due	Reduction in Franchise Tax
2011	1/30 of 1%	$76,703,328	$0
2012	1/37 of 1%	$62,191,888	$14,511,440
2013	1/50 of 1%	$46,021,997	$30,681,331
2014	1/75 of 1%	$30,681,331	$46,021,997
2015	1/150 of 1%	$15,340,665	$61,362,663
2016	None	$0	$76,703,328

ASSUMPTION (continued)

Oversight notes that corporate franchise tax collections vary from year to year; however, based on 2010 collections, Oversight assumes an estimate of the revenue reduction for the phased reduction of the franchise tax rate can be calculated as shown in the following chart. DOR officials provided total franchise tax collections of $87.5 million for the year ended June 30, 2010.

Year	Franchise Tax Rate	Franchise Tax Due	Reduction in Franchise Tax
2011	1/30 of 1%	$87,500,000	$0
2012	1/37 of 1%	$70,945,946	$16,554,054
2013	1/50 of 1%	$52,500,000	$35,000,000
2014	1/75 of 1%	$35,000,000	$52,500,000
2015	1/150 of 1%	$17,500,000	$70,000,000
2016	None	$0	$87,500,000

Oversight assumes that the franchise tax provisions in this proposal would have a fiscal impact on the General Revenue Fund beginning in FY 2012, since corporations with tax years beginning in January, 2011 would file tax returns in FY 2012 for those tax years.

Amendment 1

These provisions would limit a corporation's annual tax liability to the amount of franchise tax liability of such corporation for the year ending on or before December 31, 2010. If the corporation had no annual franchise tax liability for the year ending on or before December 31, 2010 because such corporation was not in existence or doing business in Missouri, the annual franchise tax for the first taxable year in which such corporation exists would be determined by applying the applicable tax rate to the corporation's outstanding shares and surplus if the outstanding shares and surplus exceed ten million dollars. In no case would such corporation's tax liability for any subsequent year exceed the amount of franchise tax for the first full year such corporation was in existence or doing business in Missouri.

ASSUMPTION (continued)

Officials from the **Department of Revenue** and the **Office of Administration** (shown above) included those organizations' estimate of fiscal impact for this amendment in their responses. Officials from the **University of Missouri, Economic and Policy Analysis Research Center** stated that this amendment would not change their estimate of the impact for this proposal.

Amendment 2

This amendment would allow a financial institution that is a limited liability company or limited liability partnership to claim the tax credit for such company's or partnership's annual franchise tax liability as provided in subsection 6 of this section.

Officials from the **Department of Revenue** and the **Department of Insurance, financial Institutions, and Professional Registration** stated there are currently no financial institutions organized as limited liability corporations or limited liability partnerships which pay franchise tax. Officials from the **Office of Administration, Division of Budget and Planning** included this amendment in their response and deferred to the Department of Revenue for an estimate of the fiscal impact of the amendment. Officials from the **University of Missouri, Economic and Policy Analysis Research Center** stated that they did not have the data needed to estimate the impact of this provision.

Oversight assumes this provision would have no fiscal impact.

FISCAL IMPACT - State Government	FY 2012 (10 Mo.)	FY 2013	FY 2014
GENERAL REVENUE FUND			
Reduction in future revenue - limitation on franchise tax increases *	$0	(Unknown)	(Unknown)
Revenue reduction - franchise tax rate reductions	$0	($16,554,054)	($35,000,000)
ESTIMATED NET EFFECT ON GENERAL REVENUE FUND *	**$0**	**($16,554,054 to Unknown)**	**($35,000,000 to Unknown)**

* Including unknown estimated future revenue foregone.

FISCAL IMPACT - Local Government	FY 2012 (10 Mo.)	FY 2013	FY 2014
	$0	**$0**	**$0**

FISCAL IMPACT - Small Business

This proposal would impact those small businesses which are currently subject to the franchise tax.

FISCAL DESCRIPTION

The proposed legislation would phase out the corporate franchise tax over five years and limit the franchise tax to the amount due in 2010 or in the first year the corporation is in existence or does business in the state.

This legislation is not federally mandated, would not duplicate any other program and would not require additional capital improvements or rental space.

SOURCES OF INFORMATION

Office of Administration
Division of Budget and Planning
Department of Insurance, Financial Institutions, and Professional Registration
Department of Revenue
University of Missouri
Economic and Policy Analysis Research Center

Mickey Wilson

Mickey Wilson, CPA
Director
March 1, 2011