COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 0336-02
Bill No.: Perfected SCS for SB 19
Subject: Corporations; Revenue Dept; Taxation and Revenue - General
Type: Original
Date: February 8, 2011

Bill Summary: Would limit a corporation's franchise tax liability to the previous year's tax or to the corporation's first year franchise tax in the case of a new corporation, and would phase out the corporate franchise tax over five years.

FISCAL SUMMARY

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

* Includes unknown estimated future revenue foregone.

Numbers within parentheses: ( ) indicate costs or losses.
This fiscal note contains 11 pages.

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**

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

SCS for SB 19

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.

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.

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.

ASSUMPTION (continued)

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

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 also provided actual total franchise tax collections of $87.5 million for the year ended June 30, 2010.

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 $26,712, based on 1,008 FTE hours.

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.

ASSUMPTION (continued)

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 this proposal can be calculated as shown in the following chart.

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

Amendment 2

These provisions would limit a corporation's annual franchise tax liability for all years beginning on or after January 1, 2011 to the amount of the corporation's franchise tax liability for the year ended December 31, 2010. If the corporation was not in existence in 2010, that corporation's franchise tax liability could not exceed its franchise tax liability for its first full year of business in Missouri.

In response to similar provisions in SCS for SB 18, LR 0285-04, officials from the **Office of Administration, Division of Budget and Planning** (BAP) assumed these provisions would not result in additional costs or savings to their organization.

The provisions would cap the maximum corporate franchise payment per corporation at the level the corporation paid in tax year 2010. The proposal would reduce general and total state revenues; however, BAP deferred to the Department of Revenue for an estimate of reduced revenues.

ASSUMPTION (continued)

Officials from the **University of Missouri, Economic Policy Analysis and Research Center** (EPARC) assumed that similar provisions in SCS for SB 18, LR 0285-04 would cap annual corporate franchise tax at the amount paid in the 2010 tax year for existing corporations, and cap franchise taxes for new corporations at the corporation's first year amount. EPARC officials estimated the fiscal impact of the proposal as follows.

Using the latest data available for Missouri corporations (2008), we estimate that in 2010 total franchise tax due would be $76,703,327.94. If this proposal was enacted, we would not see an increase for 2011 in franchise tax due for existing corporations, and there would be no impact on Net General Revenue due to this proposal.

Regarding new corporations, the impact would depend on the number and the tax base associated with each new corporation. Both would involve forecasts. It should be noted that the forecast for the tax base of new corporations is shifted to zero. For new corporations in Missouri after 2010, there would be an incentive to legally report no tax base. Since their future tax liabilities are limited to the first year's franchise tax amount, entrants into the Missouri market could incorporate, report zero assets in the state for the first year, and pay no franchise tax for that first year of incorporation. In all years after the first tax reporting period, their tax liability would also be zero.

Officials from the **Department of Revenue** (DOR) assume these provisions would limit the amount of franchise tax owed by corporations and would result in a reduction in Total State Revenue.

* For years ending before December 31, 2010, the annual franchise tax would be one thirtieth of one percent of the corporation's outstanding shares and surplus if the outstanding shares and surplus exceed $10.0 million. Beginning January 1, 2011, the franchise tax would be equal to one thirtieth of one percent of the corporation's outstanding shares and surplus, but a corporation's franchise tax liability could not exceed the liability of such corporation for the taxable year ending on or before December 31, 2010.

ASSUMPTION (continued)

* If the corporation had no franchise tax liability for the taxable 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 equal to one thirtieth of one percent of the corporation's outstanding shares and surplus if the outstanding shares and surplus exceed ten million dollars, but in no case could the tax liability for any subsequent year exceed the amount of tax for the first full taxable year such corporation was in existence or doing business in Missouri.

DOR would need to make form changes, and DOR and ITSD-DOR would need to make programming changes to various tax systems.

DOR provided the following estimate of the fiscal impact to the General Revenue fund.

For the years 2002 through 2009, there was an average annual franchise tax increase of 6.23 percent. This increase was calculated on corporations that had in excess of $10 million in assets and as if all franchise taxes were paid at a rate of one thirtieth of one percent. If future franchise tax due is limited to the tax owed in the corporation's calendar year 2010 franchise tax return, the estimated negative impact would be $5.4 million in 2011, $11.3 million in 2012, $17.5 million in 2013, $24 million in 2014, and $31 million in 2015.

DOR officials also provided total franchise tax collections of $87.5 million for the year ended June 30, 2010.

DOR officials assume that one FTE Revenue Processing Technician I (Range 10, Step L) would be required for every 7,800 errors generated and one FTE Revenue Processing Technician I (Range 10, Step L) would be required for every 2,600 pieces of correspondence generated.

In summary, DOR officials provided an estimate of the administrative cost to implement these provisions including two additional FTE and the related equipment and expense, of $83,623 for FY 2012, $81,203 for FY 2013, and $82,061 for FY 2014.

ASSUMPTION (continued)

Oversight assumes that implementation of these provisions would be primarily limited to forms changes and IT processing edits, and that any additional personnel costs could be absorbed with existing resources. If unanticipated additional costs are incurred or if multiple proposals are implemented which increase the DOR workload, resources could be requested through the budget process.

DOR officials also provided an estimate of the IT cost to implement the provisions of $40,068 based on 1,512 FTE hours of programming time.

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 these provisions. If multiple bills pass which require additional staffing and duties at substantial costs, ITSD-DOR could request funding through the appropriation process.

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 that foregone potential future revenue.

Oversight assumes that these provisions 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.

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

* 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 corporate franchise tax.

FISCAL DESCRIPTION

The proposed legislation would limit a corporation's franchise tax liability to the previous year's tax or to the corporation's first year franchise tax in the case of a new corporation, and would phase out the corporate franchise tax over five years.

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

Department of Revenue
University of Missouri - Economic and Policy Analysis Research Center

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