

COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 4409-08
Bill No.: Perfected SS#2 for SB 674
Subject: Taxation and Revenue - Income, Corporations
Type: #Updated
Date: May 16, 2018
Updated for revised Department of Revenue and Office of Administration - Budget and Planning responses regarding corporate allocation methods impact

Bill Summary: This proposal modifies several provisions relating to taxation.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2019	FY 2020	FY 2021
#General Revenue	(\$14,250,000 to \$26,150,000)	(\$28,500,000 to \$52,400,000)	(\$28,500,000 to \$52,400,000)
#Total Estimated Net Effect on General Revenue	(\$14,250,000 to \$26,150,000)	(\$28,500,000 to \$52,400,000)	(\$28,500,000 to \$52,400,000)

ESTIMATED NET EFFECT ON OTHER STATE FUNDS			
FUND AFFECTED	FY 2019	FY 2020	FY 2021
Total Estimated Net Effect on <u>Other</u> 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 2019	FY 2020	FY 2021
Total Estimated Net Effect on <u>All</u> Federal Funds	\$0	\$0	\$0

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)			
FUND AFFECTED	FY 2019	FY 2020	FY 2021
Total Estimated Net Effect on FTE	0	0	0

#☒ Estimated Net Effect (expenditures or reduced revenues) expected to exceed \$100,000 in any of the three fiscal years after implementation of the act.

ESTIMATED NET EFFECT ON LOCAL FUNDS			
FUND AFFECTED	FY 2019	FY 2020	FY 2021
Local Government	\$0	\$0	\$0

FISCAL ANALYSIS

ASSUMPTION

§32.200, §143.451 - §143.471 Allocation Method

#Officials at the **Office of Administration Division of Budget and Planning (B&P)** assume this section creates a single-sales factor corporate income allocation method. Sections 32.200, 143.451, 143.461, 143.471, and 620.1350 disallow other corporate income allocation methods beginning in tax year 2019.

#Based on information provided by DOR, moving to a single-sales factor only allocation method would increase Total State Revenue and General Revenue by \$141.6 million once fully implemented, at the current corporate tax rate of 6.25%. However, Section 143.071 would reduce the corporate tax rate to 3.5% in tax year 2019. Therefore, factoring in the lower corporate tax rate, B&P estimates that this provision will increase Total State Revenue and General Revenue by \$39.7 million in FY 2019 and \$79.3 million once fully implemented.

#Officials at the **Department of Revenue (DOR)** assume these proposed sections would remove Corporate Method One - Multistate Allocation and Three Factor Apportionment and Method Two - Business Transaction Single Factor Apportionment to be replaced by the Optional Single Sales Factor Apportionment. The Department estimates that this could potentially increase state revenues by an estimated range of \$91.2 million - \$103.2 million when fully implemented.

#In the previous fiscal note response, the Department scored their numbers statically at 6.25% for the single sales factor. Based on information obtained after the previous fiscal note, the Department realized we should have been reducing the apportionment savings by the corporate tax rate proposed in the bill, and has now made that change.

#In addition, the single sales factor number only included corporations moving from three factor method to single sales factor. It did not include corporations moving from the business transaction method to the single sales factor. Given the opportunity to revise because of the information learned in the first paragraph, we also suggest revising to include an estimate for this transfer. For this estimate, the Department assumed that profits currently taxed at 50% would now be taxed between 60% - 70%.

ASSUMPTION (continued)

#These revisions are outlined separately in the table below, and combined in the #table.

Apportionment Method	Total Gain at Current Rate	Total Gain with Rate Reduction
3 Factor to Single Sales Factor	\$141.6	\$79.3
Business Transaction Method to Single Sales Factor	\$21.0 - \$42.0	\$11.8 - \$23.5

in millions

#**Oversight** is unable to verify the numbers provided by B&P and DOR. We will show the range submitted by B&P DOR.

\$143.011 Individual Income Tax Rate

Officials at the **BAP** assume this proposal clarifies that the individual income tax will not be eliminated on incomes above \$9,000 once the top income tax rate reaches 5.5%. This proposal also defines the term "net general revenue collected". B&P estimates that this section will not impact Total State Revenue or the calculation under Article X, Section 18(e).

In response to the previous version, officials at the **DOR** assumed there was no fiscal impact from this proposal.

In response to the previous version, officials at the **University of Missouri's Economic and Policy Analysis Research Center (EPARC)** assumed this proposal adds language to the modification of the income tax tables when an income bracket is eliminated. As well, it defines "Net general revenue collected" as "all revenue deposited into the general revenue fund, less refunds and revenues originally deposited into the general revenue fund but designated by law for a specific distribution or transfer to another state fund."

EPARC does not find that the language that modifies the income tax tables should have any impact on how individual income taxes are calculated. The new definition of "Net general revenue collected" may or may not expedite the revenue trigger used for determining a rate reduction and increased business income deduction within this section of individual income tax law. EPARC is unable to determine all of the state funds that draw their revenues from an initial deposit into the General Revenue Fund. Therefore, they are unable to provide an impact estimate of this bill.

ASSUMPTION (continued)

§143.071 Corporate Tax Rate

Officials at the **B&P** assume this section would reduce the corporate tax rate from the current 6.25% to 3.5% beginning with tax year 2019. Based on FY 2017 net corporate collections of \$276.2 million, B&P estimates that this provision will reduce Total State Revenue and General Revenue by \$61.8 million in FY 2019. Once fully implemented, this provision will reduce Total State Revenue and General Revenue by \$123.6 million annually.

Officials at the **DOR** assume §143.071 changes the tax imposed upon the Missouri taxable income of corporations in an amount equal to 3.5% of Missouri taxable income. The Department estimates that this could potentially decrease state revenue by an estimated \$65.85 million in FY 2019 and \$131.7 million each year.

Oversight will use the estimate provided by DOR.

§143.431 Consolidated Returns

Officials at the **B&P** assume this section states that all transactions between affiliated members shall be eliminated on the Missouri consolidated income tax return. B&P notes that under this provision some corporations filing a consolidated return may have a positive impact on their tax liability, while others may have a negative impact to their tax liability. B&P is unable to determine which impacts, in the aggregate, would be greater. Therefore, due to these data limitations, BAP cannot estimate an exact impact from this section. However, this provision may have an unknown impact on Total State Revenue and General Revenue.

<u>FISCAL IMPACT - State Government</u>	FY 2019 (10 Mo.)	FY 2020	FY 2021
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GENERAL REVENUE

#Additional Revenue - Single-Sales

Factor Allocation §§32.200, 143.451-143.471, 620.1350	\$39,700,000 to \$51,600,000	\$79,300,000 to \$103,200,000	\$79,300,000 to \$103,200,000
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Revenue Reduction Corporate Tax Rate

Reduction from 6.25% to 3.5% §143.071	<u>(\$65,850,000)</u>	<u>(\$131,700,000)</u>	<u>(\$131,700,000)</u>
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**#ESTIMATED NET EFFECT ON
GENERAL REVENUE**

<u>(\$14,250,000 to \$26,150,000)</u>	<u>(\$28,500,000 to \$52,400,000)</u>	<u>(\$28,500,000 to \$52,400,000)</u>
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<u>FISCAL IMPACT - Local Government</u>	FY 2019 (10 Mo.)	FY 2020	FY 2021
	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>

FISCAL IMPACT - Small Business

No direct fiscal impact to small businesses would be expected as a result of this proposal.

FISCAL DESCRIPTION

This act modifies several provisions relating to taxation.

INDIVIDUAL INCOME TAX - This act provides that when an income bracket is eliminated from the tax table, the top remaining tax rate shall apply to all income in excess of the second highest remaining income bracket.

This act also creates a definition for "net general revenue collected", which includes all revenue deposited into the general revenue fund, less refunds and revenues originally deposited into the general revenue fund but designated by law for a specific distribution or transfer to another state fund.

CORPORATE INCOME TAX - For all tax years beginning on or after January 1, 2019, this act reduces the corporate income tax rate from 6.25% to 3.5%. (§143.071)

This act removes the requirement that an affiliated group of corporations have fifty percent or more of its income derived from sources within this state in order to file a consolidated return, and eliminates transactions between affiliated members of the group from such consolidated return. (§143.431)

For all tax years beginning on or after January 1, 2019, this act modifies the Multistate Tax Compact by requiring corporations subject to income tax in this state to apportion and allocate income according to the income tax provisions provided in Chapter 143, and disallows the three-factor apportionment option available in the Multistate Tax Compact. (§32.200)

For all tax years beginning on or after January 1, 2019, this act modifies the law relating to the allocation and apportionment of corporate income by requiring corporations to determine their income derived from sources within this state according to the provisions of this act.

FISCAL DESCRIPTION (continued)

ALLOCABLE INCOME - Net rents and royalties from real property located in the state, and capital gains from the sale of such property, is allocable to the state. Net rents and royalties from tangible personal property are allocable to the state to the extent that the property is used in this state, or in their entirety if the corporation's commercial domicile is in this state and is not organized or taxable by the state in which the property is utilized, as described in the act. Capital gains from the sale of tangible personal property is allocable to this state if the property had a situs in the state at the time of sale, or if the corporation's commercial domicile is in this state and is not organized or taxable by the state in which the property had a situs, as described in the act. Interest and dividends are allocable to this state if the corporation's commercial domicile is in this state. Patent and copyright royalties are allocable to this state to the extent that the patent or copyright is utilized in this state, or to the extent that the patent or copyright is utilized in a state in which the corporation is not taxable and the corporation's commercial domicile is in this state.

APPORTIONABLE INCOME - All apportionable income shall be apportioned to this state by dividing the total receipts of the corporation in this state during the tax period by the total receipts of the corporation everywhere during the tax period, and multiplying such result by the net income.

Receipts from the sale of tangible personal property shall be considered in this state if the property is received in this state by the purchaser, as described in the act. Receipts from all other sales shall be considered in this state if the corporation's market for such sales is in this state, as described in the act.

In the case of certain industries where unusual factual situations produce inequitable results under the apportionment and allocation provisions of this act, the Director of Revenue shall promulgate rules for determining the apportionment and allocation factors for each such industry. In such a case, a corporation may petition the Director of Revenue, as described in the act. (§143.451, §143.455, §143.471, §620.1350)

This act provides that the method of allocation and apportionment elected by a corporation shall expire after five years, or whenever the director of revenue finds and notifies such corporation that such method does not show the income applicable to this state, whichever occurs first. After such expiration or revocation, the corporation may elect to use the same or a different method. Failure to make such an election shall constitute an election to comply with the allocation and apportionment provisions provided by the act. (§143.461)


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

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SOURCES OF INFORMATION

Department of Revenue
Office of Administration Division of Budget and Planning
University of Missouri's Economic and Policy Analysis Research Center

Ross Strobe

A handwritten signature in black ink, appearing to read "Ross Strobe", with a stylized, cursive script.

Acting Director
May 16, 2018