COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 0861-01
Bill No.: HB 296
Subject: Tax Credits; Taxation and Revenue- General; Taxation and Revenue - Income; Tax Incentives; Revenue Department
Type: Original
Date: January 20, 2017

Bill Summary: This proposal changes the laws regarding tax credits so that if the income tax rate is lowered, all tax credits are reduced proportionally.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2018	FY 2019	FY 2020
General Revenue	$0	$0 or $15,050,742	$0 or $45,152,226
Total Estimated Net Effect on General Revenue	**$0**	**$0 or $15,050,742**	**$0 or $45,152,226**

Note: The fiscal note does not reflect the possibility that some of the tax credits could be utilized by insurance companies against insurance premium taxes. If this occurs, the increase in tax revenue would be split between the General Revenue Fund and the County Foreign Insurance Fund, which ultimately goes to local school districts.

ESTIMATED NET EFFECT ON OTHER STATE FUNDS			
FUND AFFECTED	FY 2018	FY 2019	FY 2020
Total Estimated Net Effect on Other State Funds	**$0**	**$0**	**$0**

Numbers within parentheses: ( ) indicate costs or losses.
This fiscal note contains 9 pages.

ESTIMATED NET EFFECT ON FEDERAL FUNDS			
FUND AFFECTED	FY 2018	FY 2019	FY 2020
Total Estimated Net Effect on All Federal Funds	**$0**	**$0**	**$0**

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)			
FUND AFFECTED	FY 2018	FY 2019	FY 2020
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 2018	FY 2019	FY 2020
Local Government	**$0**	**$0**	**$0**

FISCAL ANALYSIS

ASSUMPTION

Officials at the **Office of Administration's Division of Budget and Planning** (**B&P**) assume this proposal reduces the amount authorized for any and all tax credits by a percentage equal to the percentage reduction in the highest income tax rate under §143.011 and for any percentage increase under §143.022 in deductions for business income.

Beginning in 2017, SB's 509 and 496 (2014) established:

- a potential reduction to the top rate of tax in Missouri by one-tenth of a percent annually to a maximum reduction of one-half of a percent.
- a potential increase in the tax deductions for business income of five percent per year to a maximum of 25% percent.

These tax reductions only occur if the net General Revenue collected in the previous fiscal year exceeds the highest amount of net General Revenue collected in any of the three fiscal years prior to such fiscal year by at least $150 million.

This proposal would reduce any and all tax credits authorized by the same percentage as the percentage decrease in tax reductions. There is the potential for a reduction of 5.1% annually up to a maximum of 25.5%. Since the amount of tax credit authorizations vary annually, B&P has used a three-year (FY 2014, FY 2015, and FY 2016) average of authorized tax credits to estimate the impact. Assuming the maximum reduction of 5.1% annually for five years beginning with the 2018 tax year (a half-year impact in FY 2018 and FY 2024) the potential total reductions could be fully realized in FY 2024 and the total impact to tax credit authorizations could be $150,507,419 assuming the net General Revenue collections meet the specified levels in each of five consecutive fiscal years.

	Authorized Tax Credits	Potential Reduction in Tax Credit Authorizations
FY 18	$ 590,225,173	$ -
FY 19	$ 575,174,431	$ 15,050,742
FY 20	$ 545,072,947	$ 45,152,226
FY 21	$ 514,971,463	$ 75,253,710
FY 22	$ 484,869,979	$ 105,355,193
FY 23	$ 454,768,496	$ 135,456,677
FY 24	$ 439,717,754	$ 150,507,419

ASSUMPTION (continued)

The restrictions placed on incentives may also impact the state's ability to recruit and retain businesses, redevelop properties, and solicit contributions. Changes to these programs may also impact related economic activity. B&P is unable to estimate any induced revenue impacts.

This proposal could result in a direct increase of up to $150,507,419 to General and Total State Revenues and could impact the calculation under Article X, Section 18(e).

Officials at the **Department of Economic Development's Division of Workforce Development** and **Division of Business and Community Services** each assume no impact for FY 2017. The impact for FY 2018 is unknown but minimal since most tax credits are not issued and redeemed in the same year they are authorized. The impact for FY 2019 and beyond is unknown.

Officials at the **Missouri Housing Development Commission** (**MHDC**) assume this proposed change impacts both the 9% and 4% Missouri Low Income Housing Tax Credit (MOLIHTC) as well the affordable housing assistance program (AHAP); both tax credit programs administered by MHDC. This proposal triggers reductions to authorized tax credits only in the event that other changes are made; consequently, estimates for how such changes could impact the programs are difficult to provide

Officials at the **Missouri Development Finance Board** (**MDFB**) assume that based on the language within this legislation, there will be no impact to FY2017. The earliest known impact would be FY 2018 but there is no way to calculate the amount of that impact for that fiscal year and beyond. Credits issued do not impact the State Revenues until they are redeemed which can be many years after they are authorized. It is also impossible to determine how a reduction in credits could limit or prevent growth under programs that would normally create a net positive fiscal impact to the General Revenue.

Officials at the **Department of Social Services** (**DSS**) assume the Department participates in the administration of five different tax credit programs concerning donations to the following types of entities: domestic violence shelters (§135.550); maternity homes (§135.600); pregnancy resource centers (§135.630); residential treatment agencies (§135.1150); and developmental disability care providers (§135.1180). In addition, the Children's Division consults with the Director of Revenue under §135.339 relating to special needs adoption tax credits (§135.325 to §135.339).

The Division of Finance and Administrative Services assumes that the amount authorized for any and all tax credits, means the annual cap of funding per tax credit program, and would adjust the

ASSUMPTION (continued)

annual tax credit capacity per program in July as programs are notified of availability. If the individual tax credits issued to each taxpayer need to be adjusted, DSS would work with OA-ITSD using the Customer Management System to determine which tax credit certificates need to be reduced. It is possible regulations for the five tax credit programs administered by DSS would have to be updated. This work can be accomplished with existing staff.

The Division of Legal Services provides legal assistance to the Department in the drafting and promulgating of regulations relating to tax credit programs that it administers. In the event that this legislation is enacted and there is a change in tax rates, DSS will need to review and consult with DLS regarding the need for any changes in these regulations. Because of its expertise in these matters, DLS anticipates that it will be able to provide this legal assistance at current staffing levels.

Officials at the **Department of Natural Resources** assume the department's State Historic Preservation Office (SHPO) is responsible for reviewing and approving rehabilitation work for the state and federal historic preservation tax credit programs. Any changes in the tax credit structure may have an impact on the number of rehabilitation projects the SHPO reviews and approves. Additionally, with reduced number of projects, the fee assessed per tax credit that in part funds the SHPO staff salaries and expenses would also be reduced (Economic Development Advancement Fund 0783).

The Department would not anticipate a significant direct fiscal impact as a result of the changes made to the structure of the state Historic Preservation Tax Credit. However, we cannot predict the number of projects that would be applied for, given the proposed legislation to reduce the authority. DED tracts the financial side of the historic tax credit program and SHPO assists with the rehab design review; their agency is in a better position to quantify the potential economic impacts of limiting tax credits. With the threat of a reduced program there may be a rush on the available funds, bringing an increased number of projects and greater workload to the SHPO prior to August 28, 2017 as applicants scurry to secure funding and help ensure credit availability.

Officials at the **Department of Agriculture** assume that since the actual impact is unknown due to the variable nature of the implementation of the legislation, the impact in any given year could range from $0 to the elimination of the $8 million in allocation for that year.

Officials at the **Department of Insurance, Financial Institutions and Professional Registration** assume if passed and if the income tax rate is lowered, per the provisions of this bill, an unknown increase to premium tax revenues as a result of reduction of maximum

ASSUMPTION (continued)

allowable tax credits. Premium tax revenue is split 50/50 between General Revenue and County Foreign Insurance Fund except for domestic Stock Property and Casualty Companies who pay premium tax to the County Stock Fund. The County Foreign Insurance Fund is later distributed to school districts throughout the state. County Stock Funds are later distributed to the school district and county treasurer of the county in which the principal office of the insurer is located. It is unknown how each of these funds may be impacted by tax credits each year.

Officials at the **Department of Elementary and Secondary Education** (**DESE**) assume that other than the potential impact on the revenue stream of state and local governments (which our department has no means to calculate), this proposal does not impact DESE or local schools.

Officials at the **Department of Revenue** assume this will have no fiscal impact on the Department but may increase revenue over time.

Oversight notes under this proposal if there is a reduction to the highest income tax rate or an increase in business income deductions, then the authorization amount of all tax credits would be reduced by the same percentage equal to the percentage that such tax rate is reduced. Oversight, for fiscal note purposes, will use the projection offered by B&P

Oversight notes this proposal does not indicate which agency would be responsible for ensuring that the tax credit authorizations were reduced by the appropriate percentage. Given that all the credits end up being filed on a tax return filed with the DOR, Oversight would assume for fiscal note purposes only, that DOR would be responsible for the monitoring and distribution of the authorization limits.

Oversight notes when discussing tax credits they are referred to as authorized, issued and redeemed. The authorized tax credits are those in which companies apply and are approved for tax credits that will only be issued upon completion of a project. Low-Income Housing tax credits are an example, in that companies apply for the credit, they are authorized an amount but only upon completion of the project are they issued the credits. Should a project not be completed as requested, the credits issued will be reduced over those authorized. Often the issued amount is less than the authorized amount due to projects not meeting their goals.

According to the Tax Credit Report published by the Department of Revenue the tax credit amounts authorized, issued and redeemed over the last five years are listed below:

ASSUMPTION (continued)

Fiscal Year	Amount Authorized	Amount Issued	Amount Redeemed
FY 2016	$495,774,489	$391,935,500	$575,371,359
FY 2015	$643,835,361	$352,075,200	$513,311,854
FY 2014	$638,462,317	$379,747,860	$549,760,534
FY 2013	$551,900,475	$358,556,195	$512,911,235
FY 2012	$528,429,778	$416,873,032	$629,311,551
Five year average	$571,680,484	$379,837,557	$556,133,306

Oversight notes many of the tax credits allow the credits to be sold, assigned or transferred. Additionally, tax credits can often be carried forward, are not refundable, or can only be claimed a certain amount over a set number of year. Due to these varying rules, it is difficult to predict when tax credits may be redeemed by the taxpayer.

Oversight is unaware of any proposals adopted by the General Assembly that are currently expected to reduce the highest income tax rate or would increase a business income deduction in the fiscal note reporting period. Oversight notes that changes in the maximum individual income tax rate in SB 509 (2014) are contingent on a revenue threshold which may or may not be reached.

Oversight notes that some of the agencies receive fees from the tax credits and therefore, if the amount issued is lower, they could be impacted.

FISCAL IMPACT - State Government	FY 2018 (10 Mo.)	FY 2019	FY 2020
GENERAL REVENUE			
Savings - potential reduction of tax credit authorizations	$0	$0 or $15,050,742	$0 or $45,152,226
ESTIMATED NET EFFECT ON GENERAL REVENUE	**$0**	**$0 or $15,050,742**	**$0 or $45,152,226**

Note: The fiscal note does not reflect the possibility that some of the tax credits could be utilized by insurance companies against insurance premium taxes. If this occurs, the increase in tax revenue would be split between the General Revenue Fund and the County Foreign Insurance Fund, which ultimately goes to local school districts.

FISCAL IMPACT - Local Government	FY 2018 (10 Mo.)	FY 2019	FY 2020
	$0	**$0**	**$0**

FISCAL IMPACT - Small Business

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

FISCAL DESCRIPTION

This bill requires the amount of all tax credits to be reduced in proportion to a reduction in the income tax rate or an increase in the business income tax deduction.

The provisions of the bill will expire on December 31, six years from the effective date.

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 Agriculture
Department of Economic Development
  Division of Business and Community Services
  Division of Workforce Development
Department of Elementary and Secondary Education
Department of Insurance, Financial Institutions and Professional Registration
Department of Natural Resources
Department of Revenue
Department of Social Services
Missouri Development Finance Board
Missouri Housing Development Commission
Office of Administration
  Division of Budget and Planning

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