COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 4834-01
Bill No.: HB 1366
Subject: Tax Credits; Taxation and Revenue - Income; Business and Commerce; Agriculture and Animals
Type: Original
Date: February 3, 2014

Bill Summary: This proposal changes the laws regarding the deductions of certain net profits and caps the aggregate amount that the Department of Economic Development may issue for all tax credits.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2015	FY 2016	FY 2017
General Revenue	$0	(More than $447,512,150)	(More than $447,512,150)
Total Estimated Net Effect on General Revenue Fund	**$0**	**(More than $447,512,150)**	**(More than $447,512,150)**

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 2015	FY 2016	FY 2017
Total Estimated Net Effect on Other State Funds	**$0**	**$0**	**$0**

Numbers within parentheses: ( ) indicate costs or losses. This fiscal note contains 10 pages.

ESTIMATED NET EFFECT ON FEDERAL FUNDS			
FUND AFFECTED	FY 2015	FY 2016	FY 2017
Total Estimated Net Effect on All Federal Funds	**$0**	**$0**	**$0**

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)			
FUND AFFECTED	FY 2015	FY 2016	FY 2017
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 2015	FY 2016	FY 2017
Local Government	**$0**	**$0**	**$0**

FISCAL ANALYSIS

ASSUMPTION

§143.126 Change to Federal Adjusted Gross Income
This part of the proposal states that beginning on January 1, 2015, an individual income tax filer can subtract 100% of their Schedule C, Schedule E, and Schedule F incomes (as reported on the appropriate federal forms) from their Federal Adjusted Gross Income when determining their Missouri Adjusted Gross Income.

Officials at the **Office of Administration's Division of Budget and Planning** (**BAP**) assume this part of the proposal would not fiscally impact BAP.

Based on Tax Year 2011 data, BAP estimates this subtraction may reduce General and Total State Revenues by $525.4 million annually. BAP notes that there does not appear to be language requiring this income to be MO Source Income, so the estimate above is larger than in other similar bills. Further, is very difficult to identify business income from available data. If the proportion of taxable income that is business income is greater than that estimated for this analysis, then the loss of revenues will be higher. Also, BAP notes this analysis makes no attempt to quantify the loss of revenues that might occur if taxpayers alter their filing status to take advantage of the business income subtraction.

Officials at the **University of Missouri's Economic and Policy Analysis Research Center** (EPARC) assume using the Net Tax Due from the latest 2012 individual income tax data as our baseline, we find it is equal to $5,109.439 million. When we allow the aforementioned “business income” subtraction, we find that Net Tax Due is reduced to $4,358.353 million. This translates to a decrease in Net General Revenue of $751.086 million.

Oversight notes that this part of the proposal begins for tax years starting January 1, 2015, and will not impact the state until those tax returns are filed in January 2016 (FY 2016). Oversight will show the loss of revenue to the state beginning in FY 2016.

Oversight will use the EPARC estimate for this fiscal note.

ASSUMPTION (continued)

§620.031 Limitation of Tax Credits
This part of the proposal would limit the aggregate amount of tax credits issued after August 28, 2014, by the Department of Economic Development, the Missouri Housing Development Commission and the Missouri Development Finance Board to one hundred million dollars annually.

Officials at the **BAP** assume this part of the proposal would not fiscally impact BAP.

BAP notes that according to DOR's 2013 Tax Credit report, DED authorized over $530 million in tax credits, and issued over $340 million, in FY 2013. This proposal may increase General and Total State Revenues by several hundred million dollars when the impact of the change is fully felt in terms of reduced redemptions. This proposal may influence associated economic activity, but BAP does not have data to estimate the induced revenue impacts.

BAP notes there are several concerns that do not allow for a more precise estimate of the fiscal impact of this proposal, including the timing of such impact. It is unclear which agency is required to administer the $100 million cap and any subsequent allocation of available credits among the various programs, including the largest programs such as Low Income Housing, Historic Preservation, and BUILD. It is also unclear what the ultimate outline of any such allocation might be. Therefore, BAP cannot project in which years any revenue savings may be realized.

Officials from the **Department of Insurance, Financial Institutions and Professional Registration (DIFP)** state the limitation in §620.031 would have an unknown positive impact on revenue from premium taxes. It is unknown how many insurance companies will choose to participate in these 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 **Missouri Development Finance Board** assume this proposal may result in a reduction in the authorizations of their Infrastructure Development tax credit program; however it is unknown by how much.

ASSUMPTION (continued)

Officials at the **Missouri Housing Development Commission** (**MHDC**) assume that most of the impact from the changes proposed for MHDC will be experienced in future fiscal year periods due to the long range start up, construction, lease up period, and other activities required for actual redemption of the low income housing tax credits. Tax credits cannot be redeemed until these requirements have been met. There is no fiscal impact associated with low income housing tax credits until the tax credit is redeemed. It is impossible to predict with certainty the timing of future redemptions, especially since there is a carry back and carry forward provision with the state tax credit.

The proposed language honors all projects for which tax credits have been authorized and issued prior to August 28, 2014. All projects authorized for the 2014 low income housing tax credit funding cycle can be issued and ultimately redeemed without having to adhere to the aggregate $100 million cap. Subsequently, the most immediate impact to MHDC programs would begin for the 2015 funding cycle.

MHDC assumes tax credit projects authorized in FY 2014 and the first few months of FY 2015 will follow current limits; affordable housing tax credit is $11 million, 4% low income housing is $6 million ($60 million factoring in the full 10 year stream of credits) and 9% low income housing is $13.7 million ($137 million factoring in the full 10 year stream of credits). The estimated fiscal impact will be at least $30,700,000 per year - $19.7 million per year for the low income housing program plus $11 million per year for the affordable housing program.

Officials at the **Department of Economic Development** (**DED**) assume a positive impact will be the average annual tax credits issued (around $300 million) subtracted by the new cap ($100 million). Thus, an estimated savings of $200 million may occur as a result of this legislation. Therefore, DED assumes this proposal could range from $0 - $200,000,000 positive impact over the course of several years. Any positive impact may be offset by any increase in tax deductions allowed as a result of §143.126. In addition, as a result of the dramatic decrease in tax credits many of DED's programs could be affected or exhausted by the cap limit. This could result in a decrease of economic activity which may have a negative impact on Total State Revenue.

Oversight assumes the following chart reflects the current programs administered by the Department of Economic Development, including the Missouri Housing Development Commission and the Missouri Development Finance Board. The chart reflects the current annual or program cap of each tax credit as well as the annual average tax credit issuances by program.

Agency	Statute Section	Program Name	Annual or Program(P) Cap	Issue Average
DED	135.700	Wine and Grape	none	$105,845
DED	620.2000	MO Works	$106,000,000	
DED	32.100	Development (MOWorks)	part of MOWorks	$3,176,432
DED	135.535	Rebuilding Communities MOW	part of MOWorks	$1,706,277
DED	135.950	Enhanced Enterprise Zone	part of MOWorks	$5,665,033
DED	620.1875	Quality Jobs	part of MOWorks	$26,885,020
DED	135.110	Business Facility	none	$5,196,663
DED	135.200	Enterprise Zone	none	$4,030,670
MDFB	100.700	BUILD	$25,000,000	$8,918,017
DED	135.750	Film Production	$4,500,000	$1,822,925
DED	137.1018	Rolling Stock	none	never issued
DED	67.3000	Amateur Sporting Event	$3,000,000	not issued yet
DED	67.3005	Amateur Sporting Contributor	$10,000,000	not issued yet
DED	32.100	Neighborhood Assistance	$16,000,000	$9,699,804
DED	208.750	Family Development Account	$300,000	$14,000
DED	320.093	Dry Fire Hydrant	$500,000	$13,559
DED	135.545	Transportation Development	already expired	$0
DED	620.1100	Youth Opportunities	$6,000,000	$4,773,893
DED	135.400	Capital Tax	already expired	$0
DED	135.500	CAPCO	already expired	$0
DED	348.300	Seed Capital	already expired	$0
DED	620.635	New Enterprise Creation	already expired	$0

DED	620.1039	Qualified Research Tax	already expired	$0
DED	620.495	Small Business Incubator	$500,000	$174,452
DED	135.766	Guarantee Fee	already expired	$0
DED	135.300	Wood Energy	none	$3,253,294
DED	135.710	Alternative Fuel	expired	$0
DED	135.475	Neighborhood Preservation	$16,000,000	$3,425,626
MHDC	135.350	Low-Income Housing	cap is 100% federal amount	$157,438,827
MHDC	32.105	Affordable Housing	$11,000,000	$6,109,858
DED	253.545	Historic Preservation	$140,000,000	$104,031,444
DED	447.700	Brownfield (Remediation)	none	$14,416,062
DED		Brownfield (Demolition)	none	$0
DED		Brownfield (Jobs/Investment)	none	$1,547,503
DED	135.400	Community Development Corp	already expired	$0
MDFB	100.286	Infrastructure	$15,000,000	$18,770,520
MDFB	100.297	Bond Guarantee	$48,812,870 (P)	$0
DED	135.680	New Markets	$0 remaining (P)	$0
DED	99.1205	Distressed Area Land Assemblage	$10,000,000 remaining (P)	$10,439,739
DED	178.892	Community College New Jobs	$39,998,111 remaining (P)	$4,848,841
DED	620.1400	Skills Development Account	already expired	$0
DED	620.1560	Mature Worker	already expired	$0
DED	178.760	Job Retention	$39,998,111 remaining (P)	$7,109,546
		TOTAL		**$403,573,850**

JH:LR:OD

ASSUMPTION (continued)

Oversight assumes the language in this part of the proposal would reduce the existing caps on these programs to a shared total of $100 million dollars per year beginning on August 28, 2014 (FY 2015). Thus, the impact of these provisions would reduce tax credits issued from $403,573,850 to $100,000,000 per year. The difference between the average issuances and the new combined limit is $303,573,850 ($403,573,850 - $100,000,000).

For fiscal note purposes, **Oversight** will reflect a potential savings to the General Revenue Fund of "Less than $303,573,850" because of timing differences. For example, many credits have carry forward and/or carry back provisions which will skew estimates of when the credit will actually be redeemed (and impact the General Revenue Fund). Also, some projects within the above programs (i.e. Low-Income Housing) have a significant amount of lag time between the authorization of the credits, the subsequent issuance and finally the redemption. Therefore, the full impact of this $100 million limit could take several years. Therefore, Oversight will range the fiscal impact as "Less than $303,573,850.

FISCAL IMPACT - State Government	FY 2015 (10 Mo.)	FY 2016	FY 2017
GENERAL REVENUE			
Additional Revenue - reduction in the tax credits issued §620.031	$0	Less than $303,573,850	Less than $303,573,850
Revenue Reduction - reduction in Missouri taxable income §143.126	$0	($751,086,000)	($751,086,000)
ESTIMATED NET EFFECT ON GENERAL REVENUE	**$0**	**(More than $447,512,150)**	**(More than $447,512,150)**

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 2015 (10 Mo.)	FY 2016	FY 2017
	$0	**$0**	**$0**

JH:LR:OD

FISCAL IMPACT - Small Business

Small businesses could be affected by changes to the adjusted gross income and tax credit laws.

FISCAL DESCRIPTION

This bill subtracts from a taxpayer's federal adjusted gross income the net profits from a farm or business; net income from rental real estate, royalties, partnerships, S corporations, estates, trusts, residual interest in real estate investment conduits, and farm rental as determined by the Internal Revenue Code 1986 as amended from schedules C, E, and F.

Beginning August 28, 2014, the Department of Economic Development, the Missouri Housing Development Commission and the Missouri Development Finance Board must not in the aggregate approve applications for tax credits exceeding $100 million. No tax credits will be authorized beyond each tax credit's application approval caps in state law, but when in conflict, the aggregate cap must supersede the application approval cap.

Beginning August 28, 2014, the maximum annual amount of tax credits issued for all tax credit programs administered by the department, commission, and board must not exceed $100 million and must be issued on a first come first served basis. No tax credits will be authorized beyond each tax credit's issuance caps in state law, but when in conflict, the issuance caps must be superseded by the aggregate cap.

Beginning August 28, 2014, the approval of an application for a tax credit does not create a right to require the state to issue a credit if the issuance would exceed the aggregate $100 million limitation. All applications approved prior to the date that do require the state to issue a credit beyond the aggregate cap will be honored under the terms provided in state law at the time the application was approved and will not be counted against the cap. The commission and board must report to the department the tax credit applications approved and tax credits issued within one business day of the approval. The department must keep a running record of tax credit activities to ensure compliance with the limitations.

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

JH:LR:OD

SOURCES OF INFORMATION

Department of Economic Development
Department of Insurance, Financial Institutions and Professional Registration
Missouri Development Finance Board
Missouri Housing Development Commission
Office of Administration
Division of Budget and Planning
University of Missouri
Economic & Policy Analysis Research Center

Not Responding

Department of Revenue

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