

COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 5992-07
Bill No.: SCS for HB 1865
Subject: Corporations; Taxation and Revenue - Income; Taxation and Revenue - Sales and Use; Utilities
Type: Original
Date: May 7, 2014

Bill Summary: This proposal would modify provisions of law relating to allocating interstate sales for corporate income tax purposes, and would provide a sales and use tax exemption for utilities, chemicals, machinery, equipment, supplies, parts, and materials, used or consumed in the preparation of food.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2015	FY 2016	FY 2017
General Revenue	(Could exceed \$122,500,000)	(Could exceed \$144,000,000)	(Could exceed \$144,000,000)
Total Estimated Net Effect on General Revenue Fund	(Could exceed \$122,500,000)	(Could exceed \$144,000,000)	(Could exceed \$144,000,000)

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

ESTIMATED NET EFFECT ON OTHER STATE FUNDS			
FUND AFFECTED	FY 2015	FY 2016	FY 2017
School District Trust	(More than \$35,833,333)	(More than \$43,000,000)	(More than \$43,000,000)
Conservation Commission	(More than \$4,479,167)	(More than \$5,375,000)	(More than \$5,375,000)
Parks, and Soil and Water	(More than \$3,583,333)	(More than \$4,300,000)	(More than \$4,300,000)
Total Estimated Net Effect on <u>Other</u> State Funds	(More than \$43,895,833)	(More than \$52,675,000)	(More than \$52,675,000)

ESTIMATED NET EFFECT ON FEDERAL FUNDS			
FUND AFFECTED	FY 2015	FY 2016	FY 2017
Total Estimated Net Effect on <u>All</u> 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

Section 143.451, RSMo. - Corporate Income Tax on Interstate Transactions:

Officials from the **Office of Administration - Division of Budget and Planning (BAP)** assume these provisions would expand an additional method for allocating taxable corporate income. Based on updated information provided by the Department of Revenue, BAP officials estimated this provision may reduce Total State Revenues by up to \$10 million - \$15 million annually. BAP officials stated they would provide a more precise estimate as additional information becomes available.

ASSUMPTION (continued)

Officials from the **Department of Revenue (DOR)** stated these provisions would modify how a taxpayer computes the portion of income from all sources for intangible property or services for compensation in Missouri. A sale of intangible property would be considered in this state if the purchaser uses the property in this state. If the property is used in multiple states, the provisions would allocate the income pro rata to the portion of use in Missouri.

DOR officials estimated the loss to Total State Revenue from this provision could be as much as \$10 million to \$15 million annually.

In response to similar language in HCS for SB 693 LR 5185-02, DOR officials stated their calculation used 2011 information because that is the most recent year for which the Department has complete corporate information. DOR officials stated their understanding of the language in these provisions was to eliminate the current "partially within/partially without" category from the one-factor and three-factor allocation procedures and make sales either "in" or "out" of Missouri for corporate income tax reporting purposes. DOR officials also stated they assumed the new provisions would primarily apply to services.

DOR officials stated they calculated their estimate of impact by eliminating the reported "partially" sales for corporations with a cost of sales percentage under 50% for companies based in Missouri assuming those sales were services and would be reported as "outside" Missouri under the proposed language.

Oversight notes this provision includes definitions to use in allocating the taxable income from multi-state transactions to determine the taxable amount for Missouri. Oversight does not have information regarding the number or amount of transactions which might be subject to those definitions. For fiscal note purposes, Oversight will indicate a reduction in income tax revenues up to the Department of Revenue estimate of \$15 million.

ASSUMPTION (continued)

Section 144.055, RSMo. - Sales Tax Exemption for Utilities Used in Food Preparation:

Officials from the **Office of Administration - Division of Budget and Planning (BAP)** assume these provisions would exempt from sales tax various inputs to food preparation by restaurants and other food preparers. These exemptions would include the utilities, chemicals, machinery, equipment, supplies, parts and materials.

BAP officials assume the broad terms "supplies, parts, and materials" would exempt most inputs to production for the restaurants. BAP officials noted according to the Input-Output Use Tables provided by the United States Department of Commerce, Bureau of Economic Analysis, inputs from commodities are roughly 48% of the total output of the "food services..." industry.

BAP officials also noted the Department of Revenue reported taxable sales of "eating and drinking places" totaled about \$8.959 billion in 2013, and assume this provision might exempt (\$8.959 billion x 48%) = \$4.3 billion in currently taxable sales from taxation.

BAP officials provided the following table of the estimated revenue reductions, and noted actual losses may exceed this estimate since the data above does not include "convenience stores" or other miscellaneous food preparers. BAP officials also noted actual losses may be less than their estimate, to the extent sales taxes are not currently being collected on these transactions.

Fund	Sales Tax Rate	Revenue Reduction (Millions)
General Revenue	3%	\$129.0
School District Trust	1%	\$43.0
Conservation Commission	1/8%	\$5.4
Parks, and Soil and Water	1/10%	\$4.3

ASSUMPTION (continued)

Oversight has calculated the impact of a reduction in taxable sales of \$4.3 billion in the following table.

<u>Fund or entity</u>	<u>Sales Tax Rate</u>	<u>Revenue Reduction</u>	
		<u>Ten months</u>	<u>Annual</u>
General Revenue	3.000%	\$107,500,000	\$129,000,000
School District Trust	1.000%	\$35,833,333	\$43,000,000
Conservation Commission	0.125%	\$4,479,167	\$5,375,000
Parks, and Soil and Water	0.100%	\$3,583,333	\$4,300,000

Oversight has no independent information regarding the restaurant and related food industry costs which might be exempted from state and local sales and use tax by this proposal, and due to the potential impact of additional revenue losses from utilities used by convenience stores and other businesses involved in food production and preparation will assume this proposal could result in revenue reductions greater than the amounts calculated.

Oversight notes sales tax revenues in the School District Trust Fund are distributed along with other fund revenues to local school districts but will not include those distributions in this fiscal note.

Officials from the **Department of Revenue (DOR)** assume this proposal would provide an exemption from sales tax for electrical energy or gas, water, or other utilities purchased by a restaurant, cafeteria, fast food restaurant, delicatessen, bakery, grocery store, as well as machinery, equipment, parts, and material, used in the preparation of food sold to customers at a restaurant, cafeteria, fast food restaurant, bakery, grocery store, for consumption on or off the premises of the establishment. The exemption would not apply to local sales tax.

ASSUMPTION (continued)

Fiscal impact

DOR officials estimated this section would result in a reduction of Total State Revenue as much as \$20 million for the utilities exemption, and as much as \$80 million or more for the exemption on chemicals, machinery, equipment, supplies, parts, and materials.

Administrative Impact

DOR noted the Department would need to create claim forms and instructions, and assume Sales Tax would need one additional Revenue Processing Technician I for every 500 new refund claims.

The DOR estimate of cost to implement this proposal included one additional employee and the total including salary, benefits, equipment, and expenses totaled \$40,034 for FY 2015, \$41,356 for FY 2016, and \$41,783 for FY 2017.

Oversight assumes this proposal could be implemented with existing DOR staff; if unanticipated costs are incurred or if multiple proposals are implemented which increase the DOR workload, resources could be requested through the budget process.

IT impact

DOR officials provided an estimate of the IT cost to implement this proposal of \$18,346 based on 672 hours of programming to make changes to DOR systems.

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

Officials from the **Department of Agriculture** and the **Department of Economic Development - Public Service Commission** and **Office of Public Counsel** assume this proposal would have no fiscal impact on their organizations.

ASSUMPTION (continued)

Bill as a whole responses

In response to similar language in other proposals, officials from the **Office of the Secretary of State (SOS)** assume many bills considered by the General Assembly include provisions allowing or requiring agencies to submit rules and regulations to implement the act. The SOS is provided with core funding to handle a certain amount of normal activity resulting from each year's legislative session. The fiscal impact for this fiscal note to the Secretary of State's Office for Administrative Rules is less than \$2,500. The SOS recognizes that this is a small amount and does not expect that additional funding would be required to meet these costs. However, we also recognize that many such bills may be passed by the General Assembly in a given year and that collectively the costs may be in excess of what our office can sustain with our core budget. Therefore, we reserve the right to request funding for the cost of supporting administrative rules requirements should the need arise based on a review of the finally approved bills signed by the governor.

Officials from the **Joint Committee on Administrative Rules** assume this proposal would not have a fiscal impact to their organization in excess of existing resources.

<u>FISCAL IMPACT - State Government</u>	FY 2015 (10 Mo.)	FY 2016	FY 2017
GENERAL REVENUE FUND			
<u>Revenue reduction</u> - allocation of interstate sales income Section 143.451	(Up to \$15,000,000)	(Up to \$15,000,000)	(Up to \$15,000,000)
<u>Revenue reduction</u> - food preparation costs sales tax exemption Section 144.055	(More than \$107,500,000)	(More than \$129,000,000)	(More than \$129,000,000)
ESTIMATED NET EFFECT ON GENERAL REVENUE FUND	(Could exceed \$122,500,000)	(Could exceed \$144,000,000)	(Could exceed \$144,000,000)

FISCAL IMPACT - State Government
 (Continued)

FY 2015
 (10 Mo.)

FY 2016

FY 2017

**CONSERVATION COMMISSION
 FUND**

Revenue reduction - food preparation
 costs sales tax exemption
 Section 144.055

(More than
\$4,479,167)

(More than
\$5,375,000)

(More than
\$5,375,000)

**ESTIMATED NET EFFECT ON
 CONSERVATION COMMISSION
 FUND**

(More than
\$4,479,167)

(More than
\$5,375,000)

(More than
\$5,375,000)

**PARKS, AND SOIL AND WATER
 FUND**

Revenue reduction - food preparation
 costs sales tax exemption
 Section 144.055

(More than
\$3,583,333)

(More than
\$4,300,000)

(More than
\$4,300,000)

**ESTIMATED NET EFFECT ON
 PARKS, AND SOIL AND WATER
 FUND**

(More than
\$3,583,333)

(More than
\$4,300,000)

(More than
\$4,300,000)

SCHOOL DISTRICT TRUST FUND

Revenue reduction - food preparation
 costs sales tax exemption
 Section 144.055

(More than
\$35,833,333)

(More than
\$43,000,000)

(More than
\$43,000,000)

**ESTIMATED NET EFFECT ON
 SCHOOL DISTRICT TRUST FUND**

(More than
\$35,833,333)

(More than
\$43,000,000)

(More than
\$43,000,000)

<u>FISCAL IMPACT - Local Government</u>	FY 2015 (10 Mo.)	FY 2016	FY 2017
	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>

FISCAL IMPACT - Small Business

This proposal would have a direct fiscal impact to small businesses have interstate sales or which prepare food for human consumption.

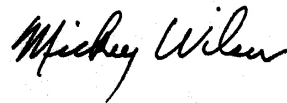
FISCAL DESCRIPTION

This proposal would provide a method for determining the portion of a corporation's interstate sales which are taxable in Missouri. The proposal would also authorize a state sales and use tax exemption for electrical energy or gas, water, or other utilities purchased by a restaurant, cafeteria, fast food restaurant, delicatessen, bakery, grocery store, as well as machinery, equipment, parts, and material, used in the preparation of food sold to customers at a restaurant, cafeteria, fast food restaurant, bakery, grocery store, for consumption on or off the premises of the establishment.

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 the Secretary of State
Joint Committee on Administrative Rules
Office of Administration
 Division of Budget and Planning
Department of Agriculture
Department of Economic Development
Department of Revenue
St. Louis County
City of Jefferson City
City of Kansas City



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May 7, 2014

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