COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 1400H.01I
Bill No.: HB 690
Subject: Taxation and Revenue - General; Tax Credits; Economic Development; Economic Development, Department of; Revenue, Department of; Education, Higher; Science and Technology; Taxation and Revenue - Income
Type: Original
Date: March 24, 2021

Bill Summary: This proposal would modify provisions relating to a tax credit for qualified research expenses.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2022	FY 2023	FY 2024
General Revenue Fund	($72,659)	Up to ($10,248,714)	Up to ($10,220,826)
Total Estimated Net Effect on General Revenue	**($72,659)**	**Up to ($10,248,714)**	**Up to ($10,220,826)**

ESTIMATED NET EFFECT ON OTHER STATE FUNDS			
FUND AFFECTED	FY 2022	FY 2023	FY 2024
Total Estimated Net Effect on Other State Funds	**$0**	**$0**	**$0**

Numbers within parentheses: () indicate costs or losses.

ESTIMATED NET EFFECT ON FEDERAL FUNDS			
FUND AFFECTED	FY 2022	FY 2023	FY 2024
Total Estimated Net Effect on All Federal Funds	**$0**	**$0**	**$0**

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)			
FUND AFFECTED	FY 2022	FY 2023	FY 2024
General Revenue – DED	1 FTE	1 FTE	1 FTE
General Revenue – DOR	Up to 3 FTE	Up to 3 FTE	Up to 3 FTE
Total Estimated Net Effect on FTE	**1 up to 4 FTE**	**1 up to 4 FTE**	**1 up to 4 FTE**

☒ Estimated Net Effect (expenditures or reduced revenues) expected to exceed $250,000 in any of the three fiscal years after implementation of the act or at full implementation of the act.

☐ Estimated Net Effect (savings or increased revenues) expected to exceed $250,000 in any of the three fiscal years after implementation of the act or at full implementation of the act.

ESTIMATED NET EFFECT ON LOCAL FUNDS			
FUND AFFECTED	FY 2022	FY 2023	FY 2024
Local Government	**$0**	**$0**	**$0**

FISCAL ANALYSIS

ASSUMPTION

Section 620.1039 – Tax Credit for Qualified Research Expenses

Officials from the **Office of Administration – Budget & Planning Division (B&P)** state this proposed legislation reauthorizes the tax credit for qualified research expenses. A taxpayer may receive a tax credit in an amount up to 10% of the excess of the taxpayer's qualified research expenses or 17% of the excess of the taxpayer's qualified research expenses if such expenses relate to research that is conducted in conjunction with a public or private college or university located in this state. This credit would have a 12 year carry forward provision. The credits may be transferred, sold, or assigned. The cap on the credits is $10 million.

General Revenue (GR) and Total State Revenue (TSR) may be reduced by an amount up to $10 million starting in Fiscal Year 2023.

The tax credit program may encourage economic activity; however, B&P cannot estimate the additional induced revenues.

This proposed legislation could impact the calculation under Article X, Section 18(e).

Officials from the **Missouri Department of Economic Development (DED)** state this proposed legislation modifies the Qualified Research Expense Tax Credit which will reduce TSR by an amount "Up to" $10 million annually.

DED states an applicant may receive a tax credit in an amount up to ten percent (10%) of the qualified research expenses. The program has a $10 million authorization cap per year.

DED assumes one (1) FTE Senior Economic Development Specialist will be needed to administer the tax credit program.

Oversight notes the prior Tax Credit for Qualified Research Expenses expired for all tax years beginning on or after January 1, 2005. Therefore, for purposes of this fiscal note, Oversight will include DED's FTE administrative cost(s), as reported by DED, less the "In-State" and "Out of State" travel costs reported as this proposed legislation does not require that DED visit, evaluate or audit any site(s).

Officials from the **Missouri Department of Revenue (DOR)** state this proposed legislation would reinstate the expired qualified research tax credit program starting January 1, 2022. The original program stopped in 2005.

This proposed legislation creates a tax credit in an amount up to 10% of the excess of the taxpayer's qualified research expense or 17% of the excess of the taxpayer's qualified research expense if those expenses are related to university research. The tax credit is not refundable but can be carried forward for twelve (12) years and imposes a cap of $10 million.

DOR notes this proposed legislation would begin in January 1, 2022 and would be claimed on the returns starting in January 2023 (Fiscal Year 2023). DOR assumes that since this proposed legislation has a cap of $10 million annually, it would be expected to be a loss to General Revenue (GR) of the $10 million.

DOR assumes one (1) FTE Associate Customer Service Representative is required for every $6,000 tax credits redeemed, one (1) Customer Service Representative for every 4,000 tax credit transfers with CISCO phones and licenses, one (1) FTE Associate Customer Service Representative for every 7,600 errors/correspondence generated and additional funds for forms and programming changes.

For purposes of this fiscal note, since the actual number of tax credit redemptions that will occur is unknown, **Oversight** will report DOR's impact "Up to" the three (3) FTE(s) estimated by DOR.

However, **Oversight** notes the first tax year in which taxpayers would qualify for the tax credit created is Tax Year 2022. Oversight notes individuals would not file their Tax Year 2022 tax returns until after January 1, 2023 (6 months **after** the beginning of Fiscal Year 2023). Therefore, Oversight will report DOR's administrative cost(s) beginning in Fiscal Year 2023 assuming DOR can hire and train such FTE(s) within the first six (6) months of Fiscal Year 2023; before Tax Year 2022 tax returns would begin to be filed claiming the tax credit created.

Officials from the **Missouri Department of Commerce and Insurance (DCI)** anticipate a potential unknown decrease of premium tax revenues (up to the tax credit limit established in the bill) as a result of the modification of the Qualified Research Tax Credit. 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 and which insurers will qualify for the tax credit.

DCI will require minimal contract computer programming to add this new tax credit to the premium tax database and can do so under existing appropriation. However, should multiple bills pass that would require additional updates to the premium tax database, DCI may need to request more expense and equipment appropriation through the budget process.

Oversight notes DCI assumes the fiscal impact of this proposed legislation can be absorbed with existing appropriation. However, should multiple bills pass that would require additional updates to DCI's premium tax database, DCI may seek additional equipment and expense appropriation through the appropriation process.

Oversight notes this proposed legislation would, beginning in Tax Year 2022, authorize a tax credit equal to ten percent (10%) of the excess of the taxpayer's qualified research expenses within this state during the tax year over the average of the taxpayer's qualified research expenses within this state over the immediately preceding three (3) tax years.

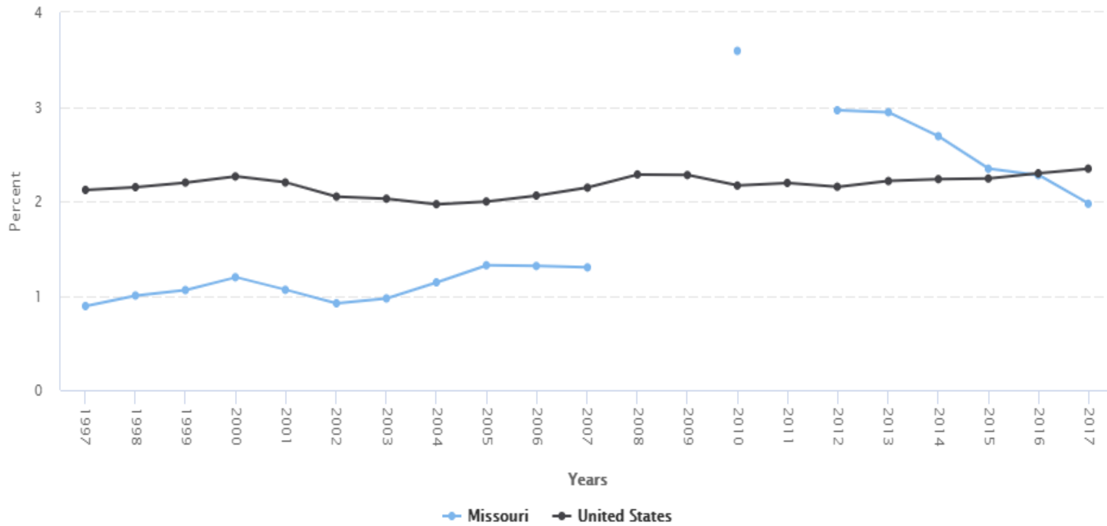
Oversight notes, should the taxpayer's qualified research expenses be related to research that is conducted in conjunction with a public or private college of or university located in this state, the tax credit authorized would be equal to seventeen percent (17%) of the excess of the taxpayer's qualified research expenses within this state during the tax year over the average of the taxpayer's qualified research expenses within this state over the immediately preceding three (3) tax years.

Oversight assumes, then, that the tax credit would be calculated similar to the following example:

<table>
<tr><th colspan="3">Tax Credit Allocation Example</th></tr>
<tr><th>Tax Year</th><th colspan="2">Total Research Expenses</th></tr>
<tr><td>2019</td><td colspan="2">$85,000,000</td></tr>
<tr><td>2020</td><td colspan="2">$96,000,000</td></tr>
<tr><td>2021</td><td colspan="2">$100,000,000</td></tr>
<tr><td></td><td>Three Year Average</td><td>$93,666,667</td></tr>
<tr><td rowspan="2">2022</td><td colspan="2">$109,000,000</td></tr>
<tr><td>Amount In Excess of Three Year Average</td><td>$15,333,333</td></tr>
<tr><td>Tax Credit</td><td>Equal to 10% or 17% of Excess</td><td>$1,533,333 or $2,606,667</td></tr>
</table>

Oversight notes, per the National Center for Science and Engineering Statistics, Missouri's business-performed research and development (as a percentage of private-industry output) recognized a continuous decline between 2012 and 2017 (the most recent year reported).

Business–Performed R&D as a Percentage of Private-Industry Output



Oversight notes the trend line(s) shown above report the business-performed research and development as a percentage of private-industry output. Thus, the assumption could be that Missouri's business-performed research and development has not truly declined; but rather Missouri's private-industry output has continuously increased by amounts greater than the increase in Missouri's business-performed research and development. The following data, however, suggests that Missouri's business-performed research and development **has** been declining.

Oversight notes, per the Missouri Economic Research and Information Center, of Missouri's overall Gross State Product (GSP) of $290,956,000,000 (chained) recognized in 2019, $258,600,000,000 was contributed by Missouri's private sector. This suggests Missouri's private sector output contributed approximately 89% to Missouri's GSP in 2019.

Assuming that Missouri's private sector contribution to Missouri's GSP is constant (89%) each year, Oversight has estimated Missouri's business-performed research and development, as a dollar amount, using Missouri's annual GSP and Missouri's business-performed research and development as a percentage of private-industry output:

Year	Missouri Chained GSP (Actual)	Estimated Private Sector Contribution To Total GSP (89%)	Missouri Research and Development - As A Percent of Private-Industry Output	**Estimated Missouri Business-Performed Research and Development ($)**
2014	$ 273,171,000,000	$ 242,792,795,474	2.69%	**$ 6,531,126,198**
2015	$ 276,700,000,000	$ 245,929,350,142	2.34%	**$ 5,754,746,793**
2016	$ 275,501,000,000	$ 244,863,685,918	2.28%	**$ 5,582,892,039**
2017	$ 278,192,000,000	$ 247,255,431,062	1.97%	**$ 4,870,931,992**

Based on the data above, Oversight assumes business-performed research and development in Missouri did decline during 2012-2017.

Based on the data above, Missouri's three (3) year average estimated business-performed research and development totals $5,956,255,010 (2014 – 2016). Based on the data above, Missouri's estimated business-performed research and development in 2017 totaled $4,870,931,992. This suggests that there would be no amount in excess of the three (3) year average to be used to calculate a tax credit.

Oversight notes, though, that the data reported above are a representation of the State of Missouri as a whole, and not each individual business.

Should the assumption be accepted that each of Missouri's individual business's research and development trends follow that of Missouri as a whole, Oversight assumes no tax credits would be authorized under this proposed legislation (u**nless research and development has increased since the last year reported**).

Oversight assumes, though, such an assumption is not likely; some businesses in Missouri may recognize increased research and development each year, even as the state, as a whole, recognizes a continuous decrease.

Since the actual amount of future tax credit authorization(s) is unknown, for purposes of this fiscal note, Oversight will report a revenue reduction to GR equal to an amount "Up to" the $10,000,000 cap beginning in Fiscal Year 2023.

FISCAL IMPACT – State Government	FY 2022 (10 Mo.)	FY 2023	FY 2024
GENERAL REVENUE FUND			
Revenue Reduction – Section 620.1039 – Tax Credit For Qualified Research Expenses	$0	Up to ($10,000,000)	Up to ($10,000,000)
Cost – DED – Section 620.1039 – Administration Of Tax Credit Program			
Personnel Services	($42,218)	($51,168)	($51,679)
Fringe Benefits	($24,199)	($29,209)	($29,382)
Equipment & Expense	($6,242)	($2,661)	($2,727)
Total Cost - DED	($72,659)	($83,038)	($83,788)
Total FTE – DED	1 FTE	1 FTE	1 FTE
Cost – DOR – Section 620.1039 – Redemption/Transfer/Error Processing Of Tax Credits		Up to…	Up to…
Personnel Services	$0	($73,811)	($74,549)
Fringe Benefits	$0	($60,731)	($60,980)
Equipment & Expense	$0	($31,134)	($1,509)
Total Cost	$0	($165,676)	($137,038)
FTE Change – DOR	0 FTE	3 FTE	3 FTE
ESTIMATED NET EFFECT ON GENERAL REVENUE	**($72,659)**	**Up to ($10,248,714)**	**Up to ($10,220,826)**

FISCAL IMPACT – Local Government	FY 2022 (10 Mo.)	FY 2023	FY 2024
	$0	**$0**	**$0**

FISCAL IMPACT – Small Business

This proposed legislation could impact any small business that qualifies for the tax credit created, as such small business could reduce or eliminate such small business's tax liability.

FISCAL DESCRIPTION

Currently, no tax credits for qualified research expenses, as defined in the bill, can be approved, awarded, or issued.

Beginning January 1, 2022, the Director of the Department of Economic Development may authorize a taxpayer a tax credit of up to 10% of the excess of a taxpayer's qualified research expenses or 17% if the research expenses relate to research that is conducted in conjunction with a public or private college or university located in this state, as certified by the Director of the Department of Economic Development, within this state during the tax year over the average of the taxpayer's qualified research expenses within this state over the immediately preceding three tax years. However, no tax credit will be allowed on that portion of the taxpayer's qualified research expenses incurred within this state during the tax year in which the credit is being claimed, to the extent such expenses exceed 200% of the taxpayer's average qualified research expenses incurred during the immediately preceding three tax years.

For tax credits that exceed the taxpayer's tax liability, the difference between the credit and the tax liability may be carried forward for 12 years.

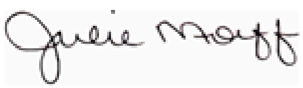
The Department Director may allow a taxpayer to transfer, sell or assign up to 40% of the tax credits issued, but not yet claimed, during any tax year commencing on or after January 1, 2021.

The annual aggregate cap on the amount of these tax credits that can be authorized by the Department of Economic Development is $10 million.

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 Administration – Budget & Planning Divisions
Missouri Department of Economic Development
Missouri Department of Revenue
Missouri Department of Commerce and Insurance



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March 24, 2021

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March 24, 2021