

BILL # HB 2147

TITLE: repeal economic development tax credits

SPONSOR: May

STATUS: As Introduced

REQUESTED BY: House

PREPARED BY: Jim Rounds, Kent Ennis

FISCAL YEAR

2001

2002

2003

REVENUES

General Fund – Corporate and Individual Income Taxes	\$-0-	Cannot be determined *
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* See Estimated Impact for further detail.

FISCAL ANALYSIS

Description

The bill eliminates 6 corporate income tax credits, and the same corresponding tax credits in the individual income tax statutes. The tax credits proposed for elimination relate to 1) increases in employment in enterprise zones, 2) increases in research and development spending, 3) property taxes paid by defense contractors, 4) employment by defense contractors, 5) increases in employment in military reuse zones, and 6) construction costs related to environmental technology facilities. The bill includes numerous technical changes to enact the proposed elimination to statute. The bill also allows for past tax credit carryforward amounts to be used in the future. The bill would become effective from and after December 31, 2001.

Estimated Impact

We believe the projected annual savings associated with the removal of these tax credits, in the long run, should equal the amount of new tax credits “earned” each year. Information on the annual amount “earned” is not readily available. Department of Revenue (DOR) reports instead list the amount of tax credits that are actually “used” each year. The latest annual estimate of “used” credits is \$15.2 million. This value may not accurately represent the total future annual savings associated with this bill since tax credit usage includes both new tax credits earned in the current year and tax credits earned in prior years but carried forward. These credits can be carried forward and used between 5 and 15 years after they are initially earned. The bill would not eliminate any of the previously earned, but unused credits. It would only affect newly earned credits.

DOR does not readily have available data on the level of “earned” credits. As a result, we cannot determine whether the total amount “earned” in each year is equal to the amount “used.” The available data is displayed in the below table.

Assumptions

DOR tax credit reports identify tax credit usage and carryforward amounts for 3 of the above 6 tax credits. Informal estimates were provided by DOR for the remaining 3 tax credits. Summing the DOR estimated credit availability for each of these tax credits, as much as \$46.8 million could be used in a single year, if company tax liability permits.

Any estimate of savings associated with this bill would be speculative. While only \$15.2 million in income tax credits were actually used in the last reported year (reported numbers were from 1996, 1997 and 1998), \$46.8 million in tax credits were available for use. The total amount available is the sum of past carryforward amounts and newly earned credits.

(Continued)

Assumptions (Continued)

The elimination of these tax credits in FY 2002 may not result in a General Fund savings in FY 2002, or even in FY 2003, because the companies that have built up large tax credit carryforward balances over the past few years will continue to use these amounts to offset their tax liability until the carryforward amounts are completely depleted, or until the carryforward timeframe runs out. The carryforward timeframes on these tax credits range from 5 years to 15 years.

Due to the uncertainty surrounding the DOR statistics (data is from as far back as tax year 1996 in some circumstances), and the uncertainty of when the corporations will ultimately run out of time or run out of their tax credit carryforward amounts, we cannot determine with certainty if the General Fund would realize any savings over the next biennium as a result of this bill.

The following table lists the name of the tax credit that is being proposed for elimination, the amount of the tax credit available for use in the last reported year, the actual usage of the tax credit in the last reported year, the last reported year, and the last reported carryforward balance. Due to confidentiality laws, DOR could not provide a separate amount for the 2 defense tax credits and the military reuse tax credit. Therefore, these are displayed in a single line in the table.

Tax Credit Summary (Includes both Corporate Income and Individual Income Tax Credits)				
<u>Tax Credit:</u>	<u>Total Available</u>	<u>Amount Used</u>	<u>Reported Year</u>	<u>Carryforward</u>
Enterprise Zones	\$5,129,900	\$2,695,900	1998	\$2,396,300
Research & Development*	\$17,000,000	\$8,900,000	1997	\$119,700,000
Construction/Environmental Technology	\$23,700,000	\$2,600,000	1996	\$21,200,000
Defense/Military Reuse**	\$1,000,000	\$1,000,000	Unknown	Unknown
Total	\$46,829,900	\$15,195,900	-	\$143,296,300

* The total available is low due to statutory restrictions. These restrictions were removed by Laws 1999, Chapter 5, 1st Special Session through a gradual phase out. When the cap on usage is completely removed (mostly impacting FY 2004), the amount available will increase.

** DOR could not provide an exact number due to confidentiality laws. However, DOR did indicate the total amount used in any one year has been less than \$1.0 million. For simplicity, we use the full \$1.0 million in this analysis for both Total Available and Amount Used.

As can be seen in the above table, even if the tax credits were immediately eliminated, over \$143.0 million in carryforward tax credits would still exist and could be used against future tax liability. For this reason, we cannot determine the exact date when the state would begin to realize the benefits from this proposed statutory change.

We do not attempt in this analysis to address the possible negative “dynamic” effects to the economy from the elimination of these tax incentives. Dynamic analysis attempts to measure the impact of tax law changes on the overall economy. Tax reduction efforts are typically associated with positive impacts on the economy, and tax increases are associated with negative impacts on the economy. The elimination of tax credits is an action that increases taxes. Therefore, some would argue that the bill would reduce economic activity and therefore overall state tax collections. However, there is little consensus about the level of this dynamic impact. The above estimates do not include an estimate for a dynamic impact to the economy from the implementation of this proposed legislation, although a negative impact is possible.

Local Government Impact

Each year local governments receive an amount equal to 15% of income tax collections from two years prior. Due to the uncertainty surrounding the timing of when state tax collections would rise as a result of this legislation, we cannot determine when the local governments would begin to feel the effects from the statutory change.