TENNESSEE GENERAL ASSEMBLY
FISCAL REVIEW COMMITTEE

FISCAL NOTE

HB 213 - SB 324

March 16, 2015

SUMMARY OF BILL: Increases, for tax years beginning on or after July 1, 2016, the weight given to the sales factor under the statutory apportionment formula used to calculate the portion of net earnings and net worth apportioned to Tennessee for franchise and excise tax purposes from a double-weighted factor to a triple-weighted factor.

ESTIMATED FISCAL IMPACT:

Decrease State Revenue – Net Impact – $33,232,400/FY16-17
$17,444,900/FY17-18
$27,438,434/FY18-19
$31,501,800/FY19-20 and Subsequent Years

Increase State Expenditures – $110,600/FY16-17

Other Fiscal Impact – Secondary economic impacts may occur as a result of this bill. Due to multiple unknown factors, fiscal impacts directly attributable to such secondary impacts cannot be quantified with reasonable certainty.

Assumptions:

- Under current law, a taxpayer's net earnings and net worth are apportioned to this state using a three-factor formula that consider the taxpayer's sales, property and payroll, with the sales factor double-weighted so that the property and payroll represent 50 percent of the apportionment factor and the sales representing the remaining 50 percent.
- The proposed legislation will, for tax years beginning on or after July 1, 2016, increase the sales factor weight from a double-weighted factor to a triple-weighted factor.
- The estimate of the fiscal impact of this bill is based on the Department of Revenue's static analysis of franchise and excise tax returns for tax periods ending in 2013. A taxpayer's tax liability will be directly impacted by the proposed change to the formula, unless 100 percent of the taxpayer's sales, property and payroll are located in Tennessee. Further, the taxpayer's tax liability will also be dependent on several other factors, including the amount of loss carryover from prior years and the amount of available tax credits.
- In general, and not accounting for loss carryovers and tax credits, increasing the sales factor weight will increase the tax liability for multi-state taxpayers where the sales factor is greater than the property and payroll factors, and will decrease the tax liability

for multi-state taxpayers where the sales factor is greater than the property and payroll factors.

- The proposed change to the formula will not have an immediate impact on the amount owed to the state for taxpayers who offset 100 percent of the tax liability as a result of loss carryovers and tax credits, particularly industrial machinery and jobs tax credits. However, since the tax base for these taxpayers, who typically have relatively larger property and payroll factors and relatively smaller sales factors, will be lower as a result of the proposed change, they will have more credits to carryover to future years.
- The Department estimates that increasing the weight of the sales factor will decrease franchise and excise tax collections by 1.65 percent, or approximately $31,501,800, per year. The Department's static analysis of franchise and excise tax returns estimates that, of 36,459 taxpayers who apportion their net earnings and net worth using the statutory formula amended by this bill, 13,100 will experience an increase in their tax liability of approximately $39,372,426 in total, 10,329 will experience a decrease in their tax liability of approximately $70,874,226 in total, and 13,030 will not experience a significant impact on their tax liability.
- Franchise and excise taxpayers are required to make estimated payments if their combined tax liability for the current year exceeds $5,000. Such estimated payments are due on the 15th day of the fourth, sixth, and ninth months of the current tax year, and on the 15th day of the first month of the succeeding year. Each estimated payment is required to be the lesser of: 25 percent of 100 percent of the combined franchise and excise tax shown on the tax return for the preceding year; or 25 percent of the combined liability for the current year.
- Since the estimated payments of taxpayers with an increased liability are only required to be 25 percent of the combined tax from the preceding year, it is assumed that these taxpayers will not increase their estimated payment in the first year. However, since the estimated payments for taxpayers with a decreased liability are only required to be 25 percent of the combined tax from the current year, it is assumed that these taxpayers will decrease their estimated payments in the first year.
- The tax years of the tax returns were used to estimate the impact of the timing of the estimated payments on tax collections.
- For the FY16-17, the decrease in state revenue will be greater than in subsequent years because the lower estimated tax payments by taxpayers with decreases in liability are not offset by higher estimated payments by taxpayers with increases in liability. However, taxpayers with increases in liability will have to make a one-time payment when the return is due in October 2017, in addition to the higher payments for the tax year beginning July 2017, thus mitigating the impact in FY17-18 and FY18-19.
- The resulting decreases in state revenue are estimated to be: $33,232,389 in FY16-17; $17,444,875 in FY17-18; $27,438,434 in FY18-19; and $31,501,800 in FY19-20 and subsequent years.
- There could be subsequent impacts on state and local government revenue and expenditures as a result of secondary economic impacts prompted by the passage of this bill. Due to multiple unknown factors, the fiscal impacts attributable to such secondary impacts cannot be quantified with reasonable certainty.
- The Department reports that there would be a one-time increase in expenditures to the Department of $110,600 in FY16-17, to accomplish all the technology changes required

by this bill. Such changes include, but are not limited to, development of new versions of the franchise and excise tax forms, new versions of the keying programs, reformat programs, debit and credit memos, and communication and testing hours in conjunction with the vendors.

CERTIFICATION:

The information contained herein is true and correct to the best of my knowledge.

Jeffrey L. Spalding, Executive Director

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