

Governor's Office Request to Model State Tax Change Proposals

Prepared by the Department of Revenue Administration

I&D Tax Rate Phase Out

The proposed request would phase out the I&D tax starting at 4% for taxable periods ending on or after 12/31/23 and reduce each tax year by 1% until reducing it to 0% for taxable periods ending on or after 12/31/27.

1. To calculate FY 2023 thru FY 2029 revenues under current law, as well as the proposed rate changes, the Department used the FY 2021 Plan of \$116,900,000 for the starting point.
2. The Department did an analysis based on prior years to break out the split of tax year revenue to fiscal year revenue. The split breakdown used for FY 2021 and forward revenue was 5% attributable to two tax years prior, 68% attributable to prior tax year, and 27% attributable to current tax year.
3. Applying the 5% tax rate to the FY 2021 Plan revenue creates a base of \$2,338,000,000 to use for the starting point.
4. The phased out rate reductions are then applied to the I&D Tax base to come up with a year-over-year and cumulative impact, as shown in the table below.
5. The fiscal impact of the proposed I&D Tax rate reduction may be overstated or understated for future fiscal years depending on whether actual revenue is more or less than FY 2021 Plan.
6. The fiscal impact does not take into account any overpayments/credit carryforwards on file. The use of these overpayments would further increase the loss in revenue as taxpayers stop making payments and supplement the payments with overpayments already on file with the Department. The Department has no way of determining how the taxpayer would utilize the overpayment, whether they would use it over the multiple years as the tax is phased out or whether they would claim it as a refund once the tax is repealed.
7. Similarly there could also be trailing amounts of I&D Tax collected even once the tax is fully repealed from audit and collection activity.

Tax Year Split and Proposed Rates

Fiscal Year	Tax Year	% Applicable to Tax Year	I&D Rates
Fiscal Year 2023	Tax Year 2021	5%	5%
	Tax Year 2022	68%	5%
	Tax Year 2023	27%	4%
Fiscal Year 2024	Tax Year 2022	5%	5%
	Tax Year 2023	68%	4%
	Tax Year 2024	27%	3%
Fiscal Year 2025	Tax Year 2023	5%	4%
	Tax Year 2024	68%	3%
	Tax Year 2025	27%	2%
Fiscal Year 2026	Tax Year 2024	5%	3%
	Tax Year 2025	68%	2%
	Tax Year 2026	27%	1%
Fiscal Year 2027	Tax Year 2025	5%	2%
	Tax Year 2026	68%	1%
	Tax Year 2027	27%	0%
Fiscal Year 2028	Tax Year 2026	5%	1%
	Tax Year 2027	68%	0%
	Tax Year 2028	27%	0%
Fiscal Year 2029 and forward	Tax Year 2027 and forward	100%	0%

Interest and Dividends Tax				
Fiscal Year	FY 2021 Plan Revenues	FY 2021 Revenues with Proposed Rate Change Phasing Out I&D	Estimated Fiscal Impact Per Year (<i>Proposed Legislation Compared to Current Law</i>)	Cumulative Fiscal Impact
2023	\$116,900,000	\$ 110,587,400	\$ (6,312,600)	\$ (6,312,600)
2024	\$116,900,000	\$ 88,376,400	\$ (22,211,000)	\$ (28,523,600)
2025	\$116,900,000	\$ 64,996,400	\$ (23,380,000)	\$ (51,903,600)
2026	\$116,900,000	\$ 44,422,000	\$ (20,574,400)	\$ (72,478,000)
2027	\$116,900,000	\$ 21,042,000	\$ (23,380,000)	\$ (95,858,000)
2028	\$116,900,000	\$ 3,039,400	\$ (18,002,600)	\$ (113,860,600)
2029	\$116,900,000	\$ -	\$ (3,039,400)	\$ (116,900,000)

BET Thresholds Increase

The proposed request would increase the BET thresholds. The BET has two filing thresholds, one measured by the taxpayer’s enterprise value tax base and one measured by the taxpayer’s gross receipts. The enterprise value tax base threshold relates directly to items that the BET taxes (interest, wages, and dividends paid or accrued), and therefore a modification to the enterprise value tax base threshold directly impacts the amount of tax collected. Alternatively, the gross receipts threshold relates to a taxpayer’s overall receipts, which may or may not include items taxable under the BET. Therefore, in many instances, a modification to the gross receipts threshold will decrease the number of BET filers, but could have minimal impact on the amount of tax actually paid. The Department analyzed increasing the BET thresholds from \$111,000 to \$250,000 for the enterprise value and \$222,000 to \$250,000 for the gross receipts applicable to taxable periods ending on or after 12/31/2022 and effective January 1, 2022.

1. To calculate the fiscal impact of the change in the BET thresholds the Department used tax year (TY) 2018 BET returns and removed any taxpayers whose enterprise value tax base was less than the \$250k threshold and/or gross receipts were less than \$250k. This revenue loss will be applicable to fiscal year 2023 and forward.
2. In TY 2018 76,781 BET returns were filed with \$234.6m BET liability reported. Of the 76,781 BET returns, 39,206 had a BET liability and 37,575 reported no BET liability. When applying the threshold change to the BET returns with no liability, the Department is unable to determine an accurate count of taxpayers who would no longer be required to file the BET return because 98% of the zero BET liability returns, below the new thresholds, do not report gross receipts and therefore it is not clear if the taxpayer would still meet the gross receipts threshold and be required to file a return with a zero liability. It is important to note that gross receipts are not required to calculate the BET, which is why the information is not consistently reported.
3. The fiscal impact of the proposed BET thresholds increase may be overstated or understated for future fiscal years depending on whether actual BET revenue is more or less than TY 2018 BET Revenue.
4. Increasing the BET thresholds will also reduce the BET credit available to offset the BPT, increasing the BPT revenue by an indeterminable amount. This will only occur when the taxpayer’s BPT liability exceeds the BET liability. For taxpayers who have a BPT liability exceeding the BET liability the estimated BET revenue loss would be offset by the increased BPT liability due to the reduced BET credit.

BET Thresholds Change					
BET Thresholds	BET Tax Revenue Lost	Count of BET Returns No Longer Filed	Count of BET Returns with a BET Liability	Count of BET Returns with No BET Liability	Count of BET Returns with No BET Liability and No Gross Receipts Reported
\$250K	(\$3,117,737)	34,780	5,027	29,753	28,950

BET Rate Decreased

The proposed request would reduce the BET rate from 0.6% to 0.55% for taxable periods ending on or after December 31, 2022.

1. To calculate FY 2021 thru FY 2024 revenues under current law as well as the proposed rate changes, the Department used the FY 2020 cash basis revenue plus the anomalous receivable revenue, reported by Department of Administrative Services in the Revenue Focus, of \$697,472,623 for the starting point (BET revenue \$258,511,460 and BPT revenue \$438,961,163).
2. As reflected in the chart below, FY 2020 included a small amount (15%) of revenue attributable to tax year (TY) 2018 which had a BPT tax rate of 7.9% and BET tax rate of 0.675%. Therefore, in order to properly calculate expected revenue under current law, a calculation was performed to adjust FY 2020 cash basis revenue to assume the lower BPT tax rate of 7.7% and BET tax rate of 0.60% for all revenue received during the fiscal year. This recalculation resulted in total expected Business Tax revenue of \$691,497,158 under current law (BET revenue \$254,202,936 and BPT revenue \$437,294,222).
3. The Department did an analysis based on prior years to break out the split of tax year revenue to fiscal year revenue. The split breakdown used for FY 2020 and forward revenue was 15% attributable to TY 2018, 63% attributable to TY 2019, and 22% attributable to TY 2020.
4. Applying the split to the FY 2020 revenue as well as applying the applicable rates creates a base of \$42,367,155,963 for BET and \$5,679,145,741 for BPT with a total Business Tax base of \$48,046,301,704 to use for the starting point.
5. The 0.55% BET rate is then applied to the BET base to come up with a year-over-year impact and cumulative impact, as shown in the table below.
6. The fiscal impact of the proposed BET rate reduction may be overstated or understated for future fiscal years depending on whether actual revenue is more or less than FY 2020 cash basis revenue plus the anomalous receivable revenue.
7. Reducing the BET rate will also reduce the BET credit available to offset the BPT, increasing the BPT revenue. Not all taxpayers have a BPT liability to be offset by a BET credit and not all taxpayer's BET liability exceeds the BPT credit. In those situations, the BET loss in revenue is not offset by an increased BPT liability. However, if a taxpayer's BPT liability exceeded the BET liability the estimated BET revenue loss would be offset by the increased BPT liability due to the reduced BET credit. To calculate an estimated impact of the reduced BET credit against the BPT, we analyzed TY 2018 comparing what percentage of BET reported was utilized against the BPT. The amount of BET

credit utilized against the BPT was 61% of the total BET reported. Applying the 61% against the BET cumulative fiscal impact in each year estimates how much BET credit would not be available to offset the BPT essentially increasing the BPT and reducing the total loss to business taxes as seen in the table below. The offset of BET losses due to the increase in BPT liability assumes that the taxpayers in question do not have BET credit carryforwards on-file that could be used to offset this added BPT liability (BET credits can be carried forward for 10 years). This means that the estimated revenue loss in the earlier years could be slightly greater due to taxpayers with increased BPT liability using up old BET credit carry forwards.

8. Lastly, combining the BET rate reduction fiscal impact with the BPT BET Credit fiscal impact results in a total impact to Business Taxes as seen in the table below.

Current Law Rates and Tax Year Split

Fiscal Year	Tax Year	% Applicable to Tax Year	BET Rates	BPT Rates
Fiscal Year 2020	Tax Year 2018	15%	0.675%	7.9%
	Tax Year 2019	63%	0.600%	7.7%
	Tax Year 2020	22%	0.600%	7.7%
Fiscal Year 2021 and forward	Tax Year 2019 and forward	100%	0.600%	7.7%

Proposed 0.55% BET and Tax Year Split

Fiscal Year	Tax Year	% Applicable to Tax Year	BET Rates	BPT Rates
Fiscal Year 2022	Tax Year 2020	15%	0.60%	7.70%
	Tax Year 2021	63%	0.60%	7.70%
	Tax Year 2022	22%	0.55%	7.70%
Fiscal Year 2023	Tax Year 2021	15%	0.60%	7.70%
	Tax Year 2022	63%	0.55%	7.70%
	Tax Year 2023	22%	0.55%	7.70%
Fiscal Year 2024 and forward	Tax Year 2023 and forward	100%	0.55%	7.70%

Fiscal Impact of 0.55% BET Rate Change to BET by Fiscal Year

BET - Static Analysis using FY 2020 Revenues				
Fiscal Year	FY 2020 Revenues with Current Law's 2019 thru 2021 Rates with no triggers enacted	FY 2020 Revenues with Proposed Legislation's Rates	Estimated Fiscal Impact Per Year <i>(Proposed Legislation Compared to Current Law)</i>	Cumulative Fiscal Impact <i>(Proposed Legislation Compared to Current Law)</i>
2022	\$254,202,936	\$249,542,549	(\$4,660,387)	(\$4,660,387)
2023	\$254,202,936	\$236,196,894	(\$13,345,654)	(\$18,006,041)
2024	\$254,202,936	\$233,019,358	(\$3,177,537)	(\$21,183,578)

Fiscal Impact of 0.55% BET Rate Change to BPT by Fiscal Year

BPT - Static Analysis using FY 2020 Revenues				
Fiscal Year	FY 2020 Revenues with Current Law's 2019 thru 2021 Rates with no triggers enacted	FY 2020 Revenues with Proposed Legislation's Rates	Estimated Fiscal Impact Per Year <i>(Proposed Legislation Compared to Current Law)</i>	Cumulative Fiscal Impact <i>(Proposed Legislation Compared to Current Law)</i>
2022	\$437,294,222	\$440,137,058	\$2,842,836	\$2,842,836
2023	\$437,294,222	\$448,277,907	\$8,140,849	\$10,983,685
2024	\$437,294,222	\$450,216,204	\$1,938,297	\$12,921,982

Fiscal Impact of 0.55% BET Rate Change to BET and BPT by Fiscal Year

Business Taxes - Static Analysis using FY 2020 Revenues				
Fiscal Year	FY 2020 Revenues with Current Law's 2019 thru 2021 Rates with no triggers enacted	FY 2020 Revenues with Proposed Legislation's Rates	Estimated Fiscal Impact Per Year <i>(Proposed Legislation Compared to Current Law)</i>	Cumulative Fiscal Impact <i>(Proposed Legislation Compared to Current Law)</i>
2022	\$691,497,158	\$689,679,607	(\$1,817,551)	(\$1,817,551)
2023	\$691,497,158	\$684,474,802	(\$5,204,805)	(\$7,022,356)
2024	\$691,497,158	\$683,235,562	(\$1,239,240)	(\$8,261,596)

M&R Tax Rate Decreased

The proposed request would reduce the M&R tax rate from 9.0% to 8.5% beginning in Fiscal Year 2022.

The DRA is unable to estimate the exact future impact of the proposed request because the Department cannot predict what the total revenues from the M&R Tax will be in future years. However, using M&R cash basis revenue data, the DRA can calculate the fiscal impact had the legislation been in place during FY 2020.

1. M&R Tax collected on a cash basis during FY 2020 was \$338,656,075, including the anomalous receivable amount from FY 2021 and the School Building Aid transfers. Operators retained commissions of \$9,143,714 (2.70% of the total collected based on data reported by Operators in FY 2020). Thus, the total tax collected by operators for FY 2020 was \$347,799,789. The FY 2020 M&R tax base was the total tax collected (\$347,799,789) divided by the tax rate of 9%, or \$3,864,442,096.
2. The FY 2020 M&R tax base is then multiplied by the new proposed 8.5% and tax rate, yielding a new estimated amount of tax collected by Operators. Using the same rate of commissions from FY 2020, the commission retained under each of the new rates is calculated and subtracted from the new liability amount. Thus, the revenue which would have been generated in FY 2020 had the reduced rate been in place is outlined in the chart below. This would be a fiscal year reduction in revenue to the General and Education Trust Funds.
3. 7,890 operators reported liability in FY 2020, all of whom would be impacted by a change in the tax rate.

Meals & Rentals Tax - Static Analysis using FY 2020 Revenues			
Proposed M&R Tax Rate	FY 2020 M&R Revenue including School Building Aid Anomalous FY 2021 Receivable and Commissions	Estimated FY Revenue under the proposed rate	Estimated Fiscal Impact Per Fiscal Year
8.5%	\$338,656,075	\$319,608,684	(\$19,047,391)