

LEGISLATIVE BUDGET BOARD
Austin, Texas

FISCAL NOTE, 78TH LEGISLATIVE REGULAR SESSION
Revision 2

March 26, 2003

TO: Honorable Ron Wilson, Chair, House Committee on Ways & Means

FROM: John Keel, Director, Legislative Budget Board

IN RE: HB694 by Davis, Yvonne (Relating to the application of the franchise tax to certain entities.),
As Introduced

Estimated Two-year Net Impact to General Revenue Related Funds for HB694, As Introduced: a positive impact of \$106,142,000 through the biennium ending August 31, 2005.

The bill would make no appropriation but could provide the legal basis for an appropriation of funds to implement the provisions of the bill.

General Revenue-Related Funds, Five-Year Impact:

Fiscal Year	Probable Net Positive/(Negative) Impact to General Revenue Related Funds
2004	\$75,192,000
2005	\$30,950,000
2006	\$31,733,000
2007	\$32,360,000
2008	\$32,862,000

All Funds, Five-Year Impact:

Fiscal Year	Probable Revenue Gain/(Loss) from <i>GENERAL REVENUE FUND</i> 1	Probable Savings/(Cost) from <i>GENERAL REVENUE FUND</i> 1
2004	\$75,192,000	\$0
2005	\$81,080,000	(\$50,130,000)
2006	\$85,785,000	(\$54,052,000)
2007	\$89,550,000	(\$57,190,000)
2008	\$92,562,000	(\$59,700,000)

Fiscal Analysis

The bill would amend Section 171.001 of the Tax Code, to tax entities with nexus to Texas that had elected to be taxed as corporations for federal tax purposes.

The businesses that would become subject to the franchise tax include business trusts and other entities that, for federal tax purposes, are classified as a corporation. To be taxable, an entity would have to engage in at least one of the following: (1) do business in this state; (2) carry on activities in this state; (3) have capital or property employed or used in this state; or (4) own property in this state, by or in the name of itself or any person, partnership, association, limited partnership, joint-stock association, or corporation. The bill would amend the definition of "corporation" to include the entities described above.

This bill would take effect January 1, 2004 for franchise tax reports originally due on or after that date.

For entities that would become subject to the tax because of the bill, income or losses occurring before January 1, 2003, could not be considered for the earned surplus component. For an entity in existence on January 1, 2003, that would have been subject to franchise tax if this bill had been effective on January 1, 2003, the first report due would be either a final report or an annual report due May 15, 2004. For entities that would have become subject to tax after January 1, 2003, if this bill had been effective January 1, 2003, the first report due would be an initial or final report, if applicable.

Methodology

This fiscal note is based on analyses provided by the Comptroller's Office, based on franchise tax file data.

The Comptroller's Office assumed that the bill would trigger an election under Article 8, Section 24 of the Texas Constitution to approve a tax on the income of natural persons. If approved in the election, two-thirds of the proceeds attributable to this bill would have to be used to provide school property tax relief, and the remaining one-third would have to be used to support education. Initial franchise tax revenue would be deposited into the General Revenue Fund. School districts would subsequently be reimbursed for property tax reductions, with resulting school district revenue remaining the same. The bill does not provide direction as to how the remaining one-third of additional revenues would be used in support of education.

The Secretary of State's office indicates that there would be an estimated 15 percent increase in the number of transactions processed by their office, at a total cost of \$208,000 in the first year of implementation and \$91,000 per year thereafter. These costs are not reflected in the above tables.

Local Government Impact

Local school district ad valorem rates would be reduced as would local property tax collections. These revenue losses would, however, be compensated for by equivalent receipts of Foundation School Fund money, after a one-year lag in accordance with current law.

Source Agencies: 304 Comptroller of Public Accounts, 307 Secretary of State

LBB Staff: JK, JO, SD, WP, CT