LEGISLATIVE BUDGET BOARD
Austin, Texas

FISCAL NOTE, 80TH LEGISLATIVE REGULAR SESSION

May 25, 2007

TO: Honorable David Dewhurst , Lieutenant Governor, Senate
Honorable Tom Craddick, Speaker of the House, House of Representatives

FROM: John S. O'Brien, Director, Legislative Budget Board

IN RE: **HB3928** by Keffer, Jim (Relating to technical changes to the revised franchise tax.),
Conference Committee Report

Estimated Two-year Net Impact to General Revenue Related Funds for HB3928, Conference Committee Report: an impact of $0 through the biennium ending August 31, 2009.

General Revenue-Related Funds, Five-Year Impact:

Fiscal Year	Probable Net Positive/(Negative) Impact to General Revenue Related Funds
2008	$0
2009	$0
2010	$0
2011	$0
2012	$0

All Funds, Five-Year Impact:

Fiscal Year	Probable Revenue Gain/(Loss) from *Property Tax Relief Fund* 304
2008	($3,502,000)
2009	$3,595,000
2010	($4,998,000)
2011	$6,568,000
2012	($3,005,000)

Fiscal Analysis

The bill would amend Chapter 171 of the Tax Code relating to the franchise tax.

The bill would modify the calculation of tax for taxable entities with total revenue between $300,000 and $900,000 by applying a sliding discount scale ranging from 80 percent for taxable entities with total revenue less than $400,000 to 20 percent for taxable entities with total revenue greater than $700,000 but less than $900,000. Under current law, taxable entities with total revenue of less than $300,000 owe no tax.

The bill would provide an optional alternative method for calculating tax for businesses with total revenue of $10 million or less. A qualified taxable entity would calculate tax by multiplying apportioned total revenue by 0.575 percent. A taxable entity electing this calculation would be eligible for the discounts for taxable entities with total revenue less than $900,000 but could not use tax credits or other adjustments.

The bill would provide an additional compensation deduction for a small employer, as defined in the Insurance Code, for initiating health care coverage for employees during the first and second year of provided coverage. For the first year, the extra deduction would be 50 percent of the employer's cost, and 25 percent for the second year.

The bill would shift forward by one year to 2010 the initial date to begin inflation-indexing the receipt levels for discount amounts and the compensation limit amount. The index would be updated in even-numbered years.

The bill would require taxable partnerships to include gross rental income instead of net rental income for determining total revenue.

The bill would provide that the gross proceeds from the sale of a loan or security treated as inventory of the seller for federal income tax purposes would be considered gross receipts for apportionment.

The bill would require a taxable entity that is a combined group to report Texas receipts for entities in the group that do not have nexus with Texas and the amount of those receipts subject to taxation in another state due to the throwback provisions.

The bill would amend the temporary credit provisions to base the credit on business loss carryforwards that existed before January 1, 2008. The bill would specify the maximum amount of usable business loss carryforwards available in any year. The bill would make the maximum credit available to a taxable entity, the annual available business loss carryforwards, multiplied by 4.5 percent. The credit amount would be limited to the liability of the taxable entity claiming the credit.

The bill would reduce the amount of control required for inclusion of a related entity in a combined group to "more than 50 percent," from 80 percent.

The bill would expand the definition of "client company" to include a client of a temporary employment service.

The bill would provide that "capital" gains from the sale of real property are included in the income that is subject to the 90 percent test for a passive entity.

The bill would create the "Business Tax Advisory Committee." Members of the committee would consist of two representatives, two senators, and at least seven residents appointed by the Comptroller. The Comptroller would serve as presiding officer. The committee would conduct a biennial study of the franchise tax and issue a report to the Legislature and the Governor at the beginning of each regular session. The provisions regarding the advisory committee would expire January 31, 2013.

With one exception, this bill would take effect January 1, 2008. SECTION 36, which would clarify the reporting responsibility of a newly taxable entity, would take effect immediately upon enactment, assuming that the bill received the requisite two-thirds majority votes in both houses of the Legislature. Otherwise, SECTION 36 would take effect September 1, 2007.

Methodology

The fiscal implications of applying discounts for taxpayers with total revenue between $300,000 and $900,000 and for the alternative tax calculation for taxpayers with less than $10 million in total revenue were estimated using data from the Internal Revenue Service. The fiscal implications of changing the first date for indexing the amounts and of the change in the ownership requirement for inclusion in a combined group were estimated using data from the Internal Revenue Service. The effect of including partnership gross rental income rather than net rental income for calculating total revenue was estimated using Internal Revenue Service data on partnerships. The effect of apportioning certain loans and securities based on gross proceeds was estimated using Comptroller franchise tax files. The effect of changing the calculation of the temporary credit provisions was estimated using Comptroller franchise tax files.

Local Government Impact

No fiscal implication to units of local government is anticipated.

Source Agencies: 304 Comptroller of Public Accounts
LBB Staff: JOB, CT, SD, SM