

LEGISLATIVE BUDGET BOARD
Austin, Texas

FISCAL NOTE, 83RD LEGISLATIVE REGULAR SESSION

March 15, 2013

TO: Honorable John Davis, Chair, House Committee On Economic & Small Business Development

FROM: Ursula Parks, Director, Legislative Budget Board

IN RE: **HB1499** by Alvarado (Relating to a franchise tax credit for certain research and development activities.), **As Introduced**

Estimated Two-year Net Impact to General Revenue Related Funds for HB1499, As Introduced: an impact of \$0 through the biennium ending August 31, 2015.

Additionally, the bill will have a direct impact of a revenue loss to the Property Tax Relief Fund of (\$40,800,000) for the 2014-15 biennium. Any loss to the Property Tax Relief Fund must be made up with an equal amount of General Revenue to fund the Foundation School Program.

General Revenue-Related Funds, Five-Year Impact:

Fiscal Year	Probable Net Positive/(Negative) Impact to General Revenue Related Funds
2014	\$0
2015	\$0
2016	\$0
2017	\$0
2018	\$0

All Funds, Five-Year Impact:

Fiscal Year	Probable Revenue (Loss) from <i>Property Tax Relief Fund</i> 304
2014	\$0
2015	(\$40,800,000)
2016	(\$49,700,000)
2017	(\$54,100,000)
2018	(\$58,700,000)

Fiscal Analysis

The bill would amend Chapter 171 of the Tax Code, regarding the franchise tax, to add new Subchapter O-1 providing a tax credit for certain research and development activities. The provisions of the bill reinstate the research and development credit that existed in the franchise tax from 2000 to 2007, including provisions for a strategic investment area and a report on the tax credit to the Legislature prior to the beginning of each regular session.

The credit for a tax period would be five percent of the sum of the excess qualified research expenses over a base period and basic research payments incurred or made in this state. The definitions for "base period", "qualified research expenses" and "basic research expenses" would follow those in federal law for the federal credit. The bill would allow a taxable entity to calculate the credit using the alternative incremental method contained in the Internal Revenue Code. The bill would allow a taxable entity to multiply by two any qualified research expenses and basic research payments made in a strategic investment area. The total amount of credit that a taxable entity could claim on any report would be limited to 50 percent of the amount of franchise tax due before other applicable credits. The limit applies to credits earned during the accounting period plus carry-forward of credit from prior years including credit earned under the credit provisions that existed prior to 2008. Credit earned during a period that cannot be used on the report for that period may be carried forward for not more than 20 consecutive reports. A taxable entity would be prohibited from transferring the credit to another taxable entity.

The strategic investment area would consist of (1) counties in the state with higher than average unemployment and below average per capita income; (2) areas in the state that are federally designated urban enterprise communities or urban enhanced enterprise communities; or (3) defense economic readjustment zones designated in the Government Code. The bill would require the Comptroller to determine the areas that qualify as strategic investment areas not later than September 1st of each year, and publish a list and a map of the designated area by October 1st of each year. The area designated would be effective for the following calendar year.

The report to the Legislature required by the bill would cover various aspects of the credit including the total amount of expenses and payment incurred, the total amount of credits applied against the tax, the amount of tax due before and after the application of the credit, the average percentage reduction in franchise tax due, the percentage of tax credits that were earned by taxable entities with fewer than 100 employees, the two-digit industrial classification of taxable entities claiming the credit, the geographical distribution of expenses and payments, the effect of the credit on the amount of research and development performed in this state, and the effect of the credit on capital investment, personal income, and state taxes. The final report prior to the expiration of the credit provisions would be required to include historical information on the credit. The report could not contain any information that is confidential by law. The Comptroller could require taxable entities that claim a credit to provide information needed for the report.

The Comptroller would be required to adopt rules and forms to implement the credit.

The credit provisions added by this bill would expire on December 31, 2022. The expiration would not affect the carry-forward of credit following the expiration date.

The bill would amend the Insurance Code and Chapter 313 of the Tax Code to incorporate the definition of strategic investment areas contained in this bill.

The bill would take effect on January 1, 2014.

Methodology

The estimated fiscal impact on the franchise tax is based on the prior research and development tax credit that existed from 2000 to 2007. Adjustments were made for the growth of the economy and the provisions of the revised franchise tax. There would be no fiscal impact in 2014 since research and development activities occurring on or after the effective date would be reported on a return due in fiscal year 2015 or later. There would be no impact from the provisions related to the strategic investment area in 2014 or 2015 since the first designation of the strategic investment area after the effective date of the bill would occur on October 1, 2014, and apply to activity during calendar year 2015. Such activity would be reported on a return due in 2016 or later.

There would be no fiscal impact from the amendment to the Insurance Code. The fiscal impact of the amendment to Chapter 313 of the Tax Code cannot be determined since the composition of the strategic investment area is unknown.

Technology

The Comptroller indicates there would be funds needed for processing credit returns, programming, and system support costs related to the research and development franchise tax credit.

Local Government Impact

No fiscal implication to units of local government is anticipated.

Source Agencies: 304 Comptroller of Public Accounts

LBB Staff: UP, RB, SD, KK