

## **BILL ANALYSIS**

Senate Research Center  
86R490 CJC-D

S.B. 1143  
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Finance  
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### **AUTHOR'S / SPONSOR'S STATEMENT OF INTENT**

The inventory tax is levied on the value of a company's inventory, and thus is especially harmful to large retail stores and other businesses that store large amounts of merchandise. It is a regressive tax in that, when a retail store's sales are lower and thus there is more inventory on the shelves, it is taxed at a higher rate than it is during periods when sales are high and there is less unsold inventory on the shelves. Inventory taxes are highly distortionary because they force companies to make decisions about production that are not entirely based on economic principles, but rather on how to pay the least amount of tax on goods produced. The tax is extremely difficult to fairly enforce because it is based on a single snapshot of a retailer's inventory on a certain date each year, which may or may not be indicative of the retailer's actual average inventory throughout the entire year.

This unnecessary burden creates strong incentives for retailers to locate their inventory outside of Texas and instead place it in states where they can avoid these harmful taxes. The tax is outdated in that Texas is one of a small and shrinking number of remaining states (less than 10) that levy an inventory tax. The State of Indiana recently phased out its property tax on inventory, and in doing so found that for every drop in its inventory tax, inventories held in that state increased.

Under S.B. 1143, a business would render two values: the snapshot inventory valuation they currently use, and an alternative value that is similar to the alternate valuation system used for autos and heavy machinery. This valuation method defines the taxable market value of a retailer's retail inventory on January 1 as the total annual sales, less sales at wholesale and sales to retailers, for the 12-month period corresponding to the preceding tax year, divided by 12. The business would pay the local taxing authorities the amount that is midway between those two valuations. The state would then provide a franchise tax credit for the difference in what the company paid and what it would have paid under the alternate valuation method.

In practice, under this plan the local taxing entities would receive less from a business in the amount of half of the difference in the current value and the alternate value, and the state would pay the other half of that difference. The company would save the full difference in the two valuations. Smaller companies that do not pay franchise tax and therefore determine they do not have need for the credit would be authorized to sell or assign their margin tax credits to larger companies that do pay the franchise tax, so that all businesses will benefit. This will result in tax savings for all retail businesses, and ultimately lead to additional growth in the state.

As proposed, S.B. 1143 amends current law relating to the appraisal for ad valorem tax purposes of tangible personal property held for sale at retail and a franchise tax credit based on the ad valorem taxes paid on such property.

### **RULEMAKING AUTHORITY**

Rulemaking authority is expressly granted to the comptroller of public accounts of the State of Texas in SECTION 2 (Section 23.1244, Tax Code) and SECTION 3 (Section 171.707, Tax Code) of this bill.

## **SECTION BY SECTION ANALYSIS**

SECTION 1. Amends Sections 23.12(a) and (f), Tax Code, as follows:

(a) Provides that except as provided by Sections 23.121 (Dealer's Motor Vehicle Inventory; Value), 23.124 (Dealer's Vessel and Outboard Motor Inventory; Value), 23.1241 (Dealer's Heavy Equipment Inventory; Value), 23.1244, and 23.127 (Retail Manufactured Housing Inventory; Value), the market value of an inventory is the price for which it would sell as a unit to a purchaser who would continue the business, rather than except as provided by Sections 23.121, 23.1241, 23.124, and 23.127, the market value of an inventory is the price for which it would sell as a unit to a purchaser who would continue the business.

(f) Authorizes the owner of an inventory other than a dealer's motor vehicle inventory as that term is defined by Section 23.121, a dealer's vessel and outboard motor inventory as that term is defined by Section 23.124, a dealer's heavy equipment inventory as that term is defined by Section 23.1241, a retail inventory as that term is defined by Section 23.1244, or a retail manufactured housing inventory as that term is defined by Section 23.127 to elect to have the inventory appraised at its market value as of September 1 of the year preceding the tax year to which the appraisal applies by filing an application with the chief appraiser requesting that the inventory be appraised as of September 1. Makes a nonsubstantive change.

SECTION 2. Amends Subchapter B, Chapter 23, Tax Code, by adding Section 23.1244, as follows:

Sec. 23.1244. RETAILER'S RETAIL INVENTORY; VALUE. (a) Defines "chief appraiser," "declaration," "retail inventory," "retailer," "sales price," and "total annual sales" for purposes of this section.

(b) Requires the chief appraiser, for the purpose of the computation of property tax, to determine the market value of a retailer's retail inventory on January 1 to be the average of the following amounts:

(1) the market value of the retail inventory on that date as determined under Section 23.12 (Inventory); and

(2) the retailer's total annual sales, less sales at wholesale and sales to other retailers, for the 12-month period corresponding to the preceding tax year, divided by 12.

(c) Requires the chief appraiser, for the purpose of the computation of property tax on the market value of the retail inventory of an owner who was not a retailer on January 1 of the preceding tax year, to estimate the amount described by Subsection (b)(2). Requires the chief appraiser, in making the estimate required by this subsection, to use sales data, if available, generated by sales from the retailer's retail inventory in the preceding tax year.

(d) Provides that except for retail inventory, tangible personal property held by a retailer is appraised as provided by the other sections of this code. Requires the chief appraiser, in the case of a retailer whose sales from the retailer's retail inventory are made predominately to other retailers, to appraise the retailer's retail inventory as provided by Section 23.12.

(e) Provides that a retailer is presumed to be an owner of retail inventory on January 1 if, in the 12-month period ending on December 31 of the preceding year, the retailer sold an item of retail inventory to a person other than a retailer. Provides that the presumption is not rebutted by the fact that a retailer has no item

of retail inventory physically on hand for sale from the retailer's retail inventory on January 1.

(f) Requires the comptroller of public accounts of the State of Texas (comptroller) by rule to adopt a retailer's retail inventory declaration form. Requires each retailer, not later than April 15 of each year, or, in the case of a retailer who was not in business on January 1, not later than 30 days after commencement of business, to file a declaration with the chief appraiser for each location at which the retailer's retail inventory to be appraised as provided by this section is located. Provides that the declaration is in addition to the rendition statement or property report filed by the retailer when rendering the retailer's retail inventory under Chapter 22. Provides that the declaration is sufficient to comply with this subsection if it sets forth the name and business address of each location at which the retailer's retail inventory to be appraised as provided by this section is located, a statement that the retailer is the owner of retail inventory, and the retailer's total annual sales, less sales at wholesale and sales to other retailers, for the 12-month period corresponding to the preceding tax year.

(g) Authorizes the chief appraiser, as provided by this subsection, to examine the books and records of a retailer. Requires a request made under this subsection to be made in writing, be delivered personally to the custodian of the records at a location at which the retailer conducts business, provide a period of not less than 15 days for the person to respond to the request, and state that the person to whom the request is addressed has the right to seek judicial relief from compliance with the request. Authorizes the chief appraiser, in a request made under this section, to examine documentation appropriate to allow the chief appraiser to ascertain the applicability of this section to the person, and sales records to substantiate information set forth in the declaration filed by the retailer.

(h) Provides that a retailer who fails to timely file a declaration under Subsection (f) in a tax year waives any right to have the retailer's retail inventory appraised as provided by this section in that tax year, and the chief appraiser is required to appraise the retailer's retail inventory as provided by Section 23.12.

(i) Provides that Section 23.123 (Declarations and Statements Confidential) applies to a declaration filed under this section in the same manner in which that section applies to a declaration filed as required by Section 23.121.

SECTION 3. Amends Chapter 171, Tax Code, by adding Subchapter N, as follows:

SUBCHAPTER N. TAX CREDIT FOR BUSINESS AD VALOREM TAX PAYMENTS  
ON INVENTORY

Sec. 171.701. DEFINITIONS. Defines "qualified entity," "retail inventory," and "retailer" for the purposes of this section.

Sec. 171.702. ELIGIBILITY FOR CREDIT. Provides that a qualified entity is eligible to apply for a credit in the amount and under the conditions and limitations provided by this subchapter against the tax imposed under this chapter.

Sec. 171.703. AMOUNT OF CREDIT; LIMITATIONS. (a) Subject to Subsection (b), the total amount of the credit under this subchapter is equal to the difference between the following amounts:

- (1) the amount of the ad valorem taxes paid by the qualified entity during the period on which a report is based that are derived from the taxable value of the entity's retail inventory; and
- (2) the amount of the ad valorem taxes the entity would have paid during the period described by Subdivision (1) on the taxable value

of the entity's retail inventory if the taxable value of that inventory were the amount determined under Section 23.1244(b)(2).

(b) Provides that a qualified entity is not eligible for a credit under this subchapter for a year in which the amount described by Subsection (a)(2) is greater than the amount described by Subsection (a)(1).

(c) Provides that the total credit claimed for a report, including the amount of any carryforward under Section 171.704, may not exceed the amount of franchise tax due for the report after all other applicable tax credits.

Sec. 171.704. CARRYFORWARD. (a) Provides that if a qualified entity is eligible for a credit that exceeds the limitation under Section 171.703(c), the entity is authorized to carry the unused credit forward for not more than three consecutive reports.

(b) Provides that a carryforward is considered the remaining portion of a credit that cannot be claimed in the current year because of the limitation under Section 171.703(c). Provides that a carryforward is added to the next year's installment of the credit in determining the limitation for that year. Provides that a credit carryforward from a previous report is considered to be used before the current year installment.

Sec. 171.705. APPLICATION FOR CREDIT. (a) Requires a qualified entity to apply for a credit under this subchapter on or with the report for the period for which the credit is claimed.

(b) Requires a qualified entity to file with a report on which the credit is claimed any information required by the comptroller to sufficiently demonstrate that the entity is eligible for the credit.

(c) Provides that the burden of establishing eligibility for and the value of the credit is on the qualified entity.

Sec. 171.706. SALE OR ASSIGNMENT OF CREDIT. (a) Authorizes a qualified entity that earns a credit under this subchapter to sell or assign all or part of the credit, and any entity to which all or part of the credit is sold or assigned to sell or assign all or part of the credit to another entity. Provides that there is no limit on the total number of transactions for the sale or assignment of all or part of the total credit authorized under this subchapter, however, collectively all transferred and retained credits claimed for a period are subject to the limitation under Section 171.703(c).

(b) Requires an entity that sells or assigns a credit under this section and the entity to which the credit is sold or assigned to jointly submit written notice of the sale or assignment to the comptroller on a form promulgated by the comptroller not later than the 30th day after the date of the sale or assignment. Requires the notice to include:

(1) the date of the sale or assignment;

(2) the amount of the credit sold or assigned;

(3) the names and federal tax identification numbers of the entity that sold or assigned the credit or part of the credit and the entity to which the credit or part of the credit was sold or assigned; and

(4) the amount of the credit owned by the selling or assigning entity before the sale or assignment, and the amount the selling or assigning entity retained, if any, after the sale or assignment.

(c) Provides that the sale or assignment of a credit in accordance with this section does not extend the period for which a credit is authorized be carried forward and does not increase the total amount of the credit that may be claimed.

Sec. 171.707. RULES. Requires the comptroller to adopt rules necessary to implement this subchapter.

SECTION 4. Provides that the legislature finds that, because of the many different types of retail inventory and the differences in the period of time that items comprising different types of retail inventory are held for sale by retailers before being sold to purchasers, it is difficult to establish a method that reliably determines the market value of such inventory. Provides that, accordingly, the legislature has enacted Section 23.1244, Tax Code, to specify a fair and accurate method for determining the appraised value of retail inventory that recognizes the unique characteristics of different types of retail inventory that may affect its value.

SECTION 5. Makes application of Section 23.1244, Tax Code, as added by this Act, prospective.

SECTION 6. Makes application of Subchapter N, Chapter 171, Tax Code, as added by this Act, prospective to January 1, 2021.

SECTION 7. Effective date: January 1, 2020.