LEGISLATIVE BUDGET BOARD
Austin, Texas

FISCAL NOTE, 88TH LEGISLATIVE REGULAR SESSION

March 21, 2023

TO: Honorable Joan Huffman, Chair, Senate Committee on Finance

FROM: Jerry McGinty, Director, Legislative Budget Board

IN RE: **SB5** by Parker (relating to an exemption from ad valorem taxation of a portion of the appraised value of tangible personal property that is held or used for the production of income and a franchise tax credit for the payment of certain related ad valorem taxes.), **Committee Report 1st House, Substituted**

Estimated Two-year Net Impact to General Revenue Related Funds for SB5, Committee Report 1st House, Substituted : a negative impact of ($109,215,217) through the biennium ending August 31, 2025.

Additionally, the bill will have a direct impact of a revenue loss to the Property Tax Relief Fund of ($525,000,000) for the 2024-25 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***
2024	($622,106)
2025	($108,593,111)
2026	($121,287,111)
2027	($130,072,111)
2028	($130,979,111)

All Funds, Five-Year Impact:

Fiscal Year	**Probable Savings/(Cost) from** ***General Revenue Fund*** **1**	**Probable Savings/(Cost) from** ***Foundation School Fund*** **193**	**Probable Savings/(Cost) from** ***Recapture Payments Atten Crdts*** **8905**	**Probable Revenue Gain/(Loss) from** ***Property Tax Relief Fund*** **304**
2024	($622,106)	$0	$0	$0
2025	($354,111)	($108,239,000)	$45,659,000	($525,000,000)
2026	($354,111)	($120,933,000)	$48,969,000	($525,000,000)
2027	($354,111)	($129,718,000)	$53,105,000	($525,000,000)
2028	($354,111)	($130,625,000)	$53,915,000	($525,000,000)

Fiscal Year	Probable Revenue Gain/(Loss) from School Districts	Change in Number of State Employees from FY 2023
2024	$0	5.0
2025	($161,890,000)	5.0
2026	($176,599,000)	5.0
2027	($187,192,000)	5.0
2028	($190,659,000)	5.0

Fiscal Analysis

The bill would amend Section 11.145 of the Tax Code, relating to Income-Producing Tangible Personal Property Having Value of Less Than $2,500, and exempt from taxation $25,000 of the appraised value of tangible personal property the person owns that is held or used for the production of income, rather than less than $2,500 dollars of taxable value. The exemption would apply to each separate location in each separate taxing unit and all property that has taxable situs in each separate location in the taxing unit is aggregated to determine taxable value. The exemption would apply to tangible personal property that is subject to lease.

If the person holding tangible personal property is a related business entity, all property that has taxable situs at the same location in a taxing unit would be combined with property owned by each other related business enterprise to determine taxable value. The chief appraiser would investigate to determine if an entity is a related business entity.

The bill would amend Section 22.01 of the Tax Code, relating to Rendition Generally, and add rendition requirements.

These provisions of the bill would take effect January 1, 2024, contingent on the approval by voters of a constitutional amendment (SJR 3) authorizing the legislature to grant the exemption.

The bill would amend Chapter 171 of the Tax Code, relating to the Franchise Tax by adding Subchapter N to provide a tax credit for property taxes paid on inventory.

The amount of a taxable entity's credit for a report would be equal to 20.0 percent of the amount of ad valorem taxes paid by the entity that are derived from the taxable value of the inventory owned by the entity and located in Texas, for the period on which the report is based. The total credit claimed on a report, including any carryforward credit, may not exceed 20.0 percent of the amount of franchise tax due for the report after applying all other applicable credits.

The total amount of credits that could be awarded per year may not exceed $525.0 million. If the aggregate amount of credit applied for based on 20.0 percent of property taxes imposed on taxpayers' inventory were to exceed the $525.0 million limit, the credits would be awarded by the comptroller on a pro rata basis. To the extent that credit awards for a year would remain unused due to limitation to taxpayers' franchise tax liability, the unused credit would be subject to reallocation to taxpayers with remaining franchise tax liability to ensure that the $525.0 million in credit be used.

Credits would be applied for but not taken on reports as initially filed. After proration and reallocation of the total credit budget for a report year, amounts of applicable credit by taxpayer would be refunded.

Methodology

The bill's proposed exemption of $25,000 of tangible personal property that has an aggregate value of at least $25,000 would create a cost to school districts and to the state through the operation of the school funding formulas. Unlike the de minimis $2,500 exemption in current law, which exempts tangible personal property only if the total value of such property owned is less than $2,500, the proposed change would exempt $25,000 of the appraised value of such tangible personal property regardless of the total value of such property owned.

The estimate was based on tangible personal property information reported electronically by appraisal districts. The percentage of tangible personal property accounts exceeding $25,000 in market value was identified from a sample of personal property accounts and extrapolated statewide. The value loss was calculated based on the resulting number of personal property accounts that would receive the proposed $25,000 exemption.

The cost to the Foundation School Program (FSP) due to exempting $25,000 of tangible personal property is estimated to be $108.2 million in fiscal year 2025, increasing to $130.6 million in fiscal year 2028.

The cost to the FSP includes estimated decreases in Recapture Payments - Attendance Credits of $45.7 million in fiscal year 2025, increasing to $53.9 million in fiscal year 2028 as a result of the reduction in school district taxable value. The decrease in recapture is reflected as a savings in the table above because recapture is appropriated as a method of finance for the FSP in the General Appropriations Act.

The provision for reallocation of available credit from taxpayers with insufficient franchise tax liability to exhaust the credit to taxpayers with remaining liability against which credit may be applied ensures that the annual reduction in net franchise tax collections would be $525.0 million. As the credits would not be taken on reports as originally filed but refunded after proration and reallocation following filing of reports on extensions, the amount of credit provided for a franchise tax report year would reduce net tax collections in the subsequent fiscal year.

This analysis assumes administrative costs of $622,106 in fiscal year 2024 and $354,111 in each subsequent year to administer the new franchise tax credit. The Comptroller's office anticipates needing to hire five Accounts Examiners III and to hire a contractor for application development.

Technology

The administrative cost includes a technology cost of $288,000 in fiscal 2024 to hire a contractor for one year to assist in the estimated 2,100 programming hours that would be needed to develop an application process for entities applying for the credit in this bill.

Local Government Impact

Contingent upon passage of a constitutional amendment authorizing the the exemption of business personal property from ad valorem taxation, the bill would reduce taxable value. However, the no-new-revenue and voter-approval tax rates as provided by Section 26.04, Tax Code could be higher as a consequence of the additional exemption proposed by the bill.

The fiscal impact to school districts is shown in the table above.

Source Agencies: 304 Comptroller of Public Accounts

LBB Staff: JMc, KK, SD, BRI