

COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 1400H.03C
 Bill No.: HCS for HB 690
 Subject: Taxation and Revenue - General; Tax Credits; Economic Development; Economic Development, Department of; Revenue, Department of; Education, Higher; Science and Technology; Taxation and Revenue - Income
 Type: Original
 Date: April 19, 2021

Bill Summary: This proposal would change laws regarding tax incentives.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND				
FUND AFFECTED	FY 2022	FY 2023	FY 2024	Fully Implemented (FY 2027)
General Revenue Fund	Less than or greater than (\$39,761,515)	Less than or greater than (\$89,626,425)	Less than or greater than (\$89,598,537)	Less than or greater than (\$49,916,856)
Total Estimated Net Effect on General Revenue	Less than or greater than (\$39,761,515)	Less than or greater than (\$89,626,425)	Less than or greater than (\$89,598,537)	Less than or greater than (\$49,916,856)

ESTIMATED NET EFFECT ON OTHER STATE FUNDS				
FUND AFFECTED	FY 2022	FY 2023	FY 2024	Fully Implemented (FY 2027)
Total Estimated Net Effect on Other State Funds	\$0	\$0	\$0	\$0

Numbers within parentheses: () indicate costs or losses.

ESTIMATED NET EFFECT ON FEDERAL FUNDS				
FUND AFFECTED	FY 2022	FY 2023	FY 2024	Fully Implemented (FY 2027)
Total Estimated Net Effect on All Federal Funds	\$0	\$0	\$0	\$0

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)				
FUND AFFECTED	FY 2022	FY 2023	FY 2024	Fully Implemented (FY 2027)
Total Estimated Net Effect on FTE	0	0	0	\$0

- Estimated Net Effect (expenditures or reduced revenues) expected to exceed \$250,000 in any of the three fiscal years after implementation of the act or at full implementation of the act.
- Estimated Net Effect (savings or increased revenues) expected to exceed \$250,000 in any of the three fiscal years after implementation of the act or at full implementation of the act.

ESTIMATED NET EFFECT ON LOCAL FUNDS				
FUND AFFECTED	FY 2022	FY 2023	FY 2024	Fully Implemented (FY 2027)
Local Government	\$0	\$0	\$0	\$0

FISCAL ANALYSIS

ASSUMPTION

Section 620.1039 – Tax Credit for Qualified Research Expenses

Officials from the **Office of Administration – Budget & Planning Division (B&P)** state this section reauthorizes the tax credit for qualified research expenses. A taxpayer may receive a tax credit in an amount equal to the greater of: 10% of the taxpayer's additional qualified research expenses or 17% of the taxpayer's additional qualified research expenses if such expenses relate to research conducted in conjunction with a public or private college or university located in this state. This credit would have a 12 year carry forward provision. The credits may be transferred, sold, or assigned. The cap on the credits is \$10 million, provided that \$5 million shall be reserved for minority business enterprises, women's business enterprises, and small businesses. Any reserved amount not issued or awarded to a minority business enterprise, women's business enterprise, or small business by November 1 of the tax year may be issued to any taxpayer otherwise eligible. No single taxpayer shall be issued or awarded more than \$300,000 in tax credits in any year.

General Revenue (GR) and Total State Revenue (TSR) may be reduced by up to \$10 million, starting in Fiscal Year 2023.

This program may encourage economic activity. B&P cannot estimate additional induced revenues.

The section legislation could impact the calculation under Article X, Section 18(e).

Officials from the **Missouri Department of Revenue (DOR)** state this section would reinstate the expired Qualified Research Tax Credit program starting January 1, 2022. The original program stopped in 2005.

This section creates a tax credit in an amount up to 10% of the excess of the taxpayer's qualified research expense or 17% of the excess of the taxpayer's qualified research expense if those expenses are related to university research. Starting January 1, 2022 this allows the credit to be carried forward for twelve (12) years and imposes a cap of \$10 million. This section requires that \$5 million of the credit be reserved for minority business enterprises, women's business enterprises and small businesses. Each taxpayer is limited to \$300,000 in credits.

DOR notes the tax credit program would begin in January 1, 2022 and would be claimed on the returns starting in January 2023 (Fiscal Year 2023). DOR assumes that since this section has a cap of \$10 million annually it would be expected to be a loss to GR of the \$10 million.

DOR assumes one (1) FTE Associate Customer Service Representative is required for every \$6,000 tax credits redeemed, one (1) Customer Service Representative for every 4,000 tax credit transfers with CISCO phones and licenses, one (1) FTE Associate Customer Service Representative for every 7,600 errors/correspondence generated and additional funds for forms and programming changes.

For purposes of this fiscal note, since the actual number of tax credit redemptions that will occur is unknown, **Oversight** will report DOR's impact "Up to" the three (3) FTE(s) estimated by DOR.

However, **Oversight** notes the first tax year in which taxpayers would qualify for the tax credit created is Tax Year 2022. Oversight notes individuals would not file their Tax Year 2022 tax returns until after January 1, 2023 (6 months **after** the beginning of Fiscal Year 2023). Therefore, Oversight will report DOR's administrative cost(s) beginning in Fiscal Year 2023 assuming DOR can hire and train such FTE(s) within the first six (6) months of Fiscal Year 2023; before Tax Year 2022 tax returns would begin to be filed claiming the tax credit created.

Officials from the **Missouri Department of Commerce and Insurance (DCI)** anticipate a potential unknown decrease of premium tax revenues (up to the tax credit limit established in the bill) as a result of the modification of the Qualified Research Tax Credit. Premium tax revenue is split 50/50 between General Revenue and County Foreign Insurance Fund except for domestic Stock Property and Casualty Companies who pay premium tax to the County Stock Fund. The County Foreign Insurance Fund is later distributed to school districts throughout the state. County Stock Funds are later distributed to the school district and county treasurer of the county in which the principal office of the insurer is located. It is unknown how each of these funds may be impacted by tax credits each year and which insurers will qualify for the tax credit. DCI will require minimal contract computer programming to add this new tax credit to the premium tax database and can do so under existing appropriation. However, should multiple bills pass that would require additional updates to the premium tax database, DCI may need to request more expense and equipment appropriation through the budget process.

Oversight notes DCI assumes the fiscal impact of this proposed legislation can be absorbed with existing appropriation. However, should multiple bills pass that would require additional updates to DCI's premium tax database, DCI may seek additional equipment and expense appropriation through the appropriation process.

In response to the previous version of this proposed legislation, officials from the **Missouri Department of Economic Development (DED)** stated this section modifies the Qualified Research Expense Tax Credit which will reduce TSR by an amount "Up to" \$10 million annually.

DED assumed one (1) FTE Senior Economic Development Specialist will be needed to administer the tax credit program.

Oversight notes the prior Tax Credit for Qualified Research Expenses expired for all tax years beginning on or after January 1, 2005. Therefore, for purposes of this fiscal note, Oversight will include DED’s FTE administrative cost(s), as reported by DED, less the “In-State” and “Out of State” travel costs reported as this proposed legislation does not require that DED visit, evaluate or audit any site(s).

Oversight notes this proposed legislation would, beginning in Tax Year 2022, authorize a tax credit equal to ten percent (10%) of the taxpayer’s additional qualified research expenses or, if such qualified research expenses relate to research conducted in conjunction with a public or private college or university located in this state, seventeen percent (17%) of the taxpayer’s additional qualified research expenses.

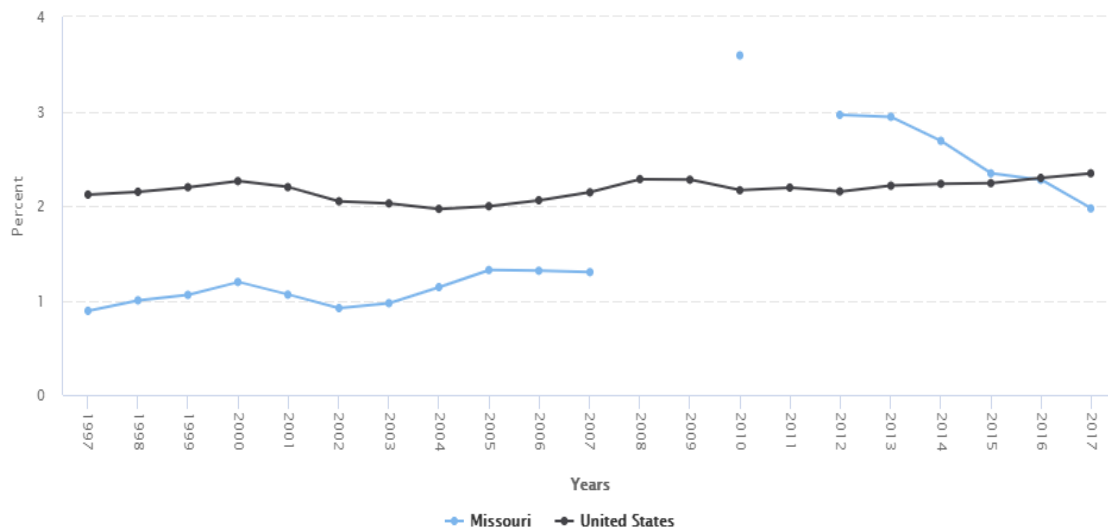
Oversight notes, “Additional Qualified Research Expenses” are defined as “the difference between qualified research expenses... incurred in a tax year subtracted by the average of the taxpayer’s qualified research expenses incurred in the three immediately preceding tax years”.

Oversight assumes, then, that the tax credit would be calculated similar to the following example:

Tax Credit Allocation Example		
Tax Year	Total Research Expenses	
2019	\$85,000,000	
2020	\$96,000,000	
2021	\$100,000,000	
	Three Year Average	\$93,666,667
2022	\$109,000,000	
	Amount In Excess of Three Year Average	\$15,333,333
Tax Credit	Equal to 10% or 17% of Excess	\$1,533,333 or \$2,606,667

Oversight notes, per the [National Center for Science and Engineering Statistics](#), Missouri’s business-performed research and development (as a percentage of private-industry output) recognized a continuous decline between 2012 and 2017 (the most recent year reported).

Business-Performed R&D as a Percentage of Private-Industry Output



Oversight notes the trend line(s) shown above report the business-performed research and development as a percentage of private-industry output. Thus, the assumption could be that Missouri’s business-performed research and development has not truly declined; but rather Missouri’s private-industry output has continuously increased by amounts greater than the increase in Missouri’s business-performed research and development. The following data, however, suggests that Missouri’s business-performed research and development **has** been declining.

Oversight notes, per the [Missouri Economic Research and Information Center](#), of Missouri’s overall Gross State Product (GSP) of \$290,956,000,000 (chained) recognized in 2019, \$258,600,000,000 was contributed by Missouri’s private sector. This suggests Missouri’s private sector output contributed approximately 89% to Missouri’s GSP in 2019.

Assuming that Missouri’s private sector contribution to Missouri’s GSP is constant (89%) each year, Oversight has estimated Missouri’s business-performed research and development, as a dollar amount, using Missouri’s annual GSP and Missouri’s business-performed research and development as a percentage of private-industry output:

Year	Missouri Chained GSP (Actual)	Estimated Private Sector Contribution To Total GSP (89%)	Missouri Research and Development - As A Percent of Private-Industry Output	Estimated Missouri Business-Performed Research and Development (\$)
2014	\$ 273,171,000,000	\$ 242,792,795,474	2.69%	\$ 6,531,126,198
2015	\$ 276,700,000,000	\$ 245,929,350,142	2.34%	\$ 5,754,746,793
2016	\$ 275,501,000,000	\$ 244,863,685,918	2.28%	\$ 5,582,892,039
2017	\$ 278,192,000,000	\$ 247,255,431,062	1.97%	\$ 4,870,931,992

Based on the data above, Oversight assumes business-performed research and development in Missouri did decline during 2012-2017.

Based on the data above, Missouri's three (3) year average estimated business-performed research and development totals \$5,956,255,010 (2014 – 2016). Based on the data above, Missouri's estimated business-performed research and development in 2017 totaled \$4,870,931,992. This suggests that there would be no amount in excess of the three (3) year average to be used to calculate a tax credit.

Oversight notes, though, that the data reported above are a representation of the State of Missouri as a whole, and not each individual business.

Should the assumption be accepted that each of Missouri's individual business's research and development trends follow that of Missouri as a whole, Oversight assumes no tax credits would be authorized under this proposed legislation (**unless research and development has increased since the last year reported**).

Oversight assumes, though, such an assumption is not likely; some businesses in Missouri may recognize increased research and development each year, even as the state, as a whole, recognizes a continuous decrease.

Since the actual amount of future tax credit authorization(s) is unknown, for purposes of this fiscal note, Oversight will report a revenue reduction to GR equal to an amount "Up to" the \$10,000,000 cap beginning in Fiscal Year 2023.

Section 1 – Corporate Income Tax

Officials from **B&P** state this section would exempt corporations within certain NAICS codes from the Corporate Income Tax for Tax Year(s) 2022 through 2026.

Based on data published by the U.S. Census Bureau, B&P estimates that this section could exempt up to 1,494 corporations located in Missouri from the Corporate Income Tax. Table 1 shows the estimated number of corporations and revenue impacted.

Table 1: Estimated number of firms and revenues

NAICS		Est. # Corporations	Est. Revenue for Corporations	Est. Exempted income (4.0% tax rate)
332992	Small arms ammunition manufacturing	3	\$229,208,100	\$9,168,324
332994	Small arms, ordinance, and ordnance accessories manufacturing	0	\$0	
541715	Research and development in the physical, engineering, and life sciences (except nanotechnology and biotechnology)	Up to 59	Up to \$367,286,682	Up to \$14,691,424
624210	Community food services	0	\$0	
624410	Child day care services	89	\$36,045,534	\$1,441,821
722511	Full-service restaurants	878	\$1,056,970,642	\$42,278,886
722513	Limited-service restaurants	465	\$294,931,830	\$11,797,273
		1,494		Up to \$79,377,711

Based on the above information, B&P estimates that this section could reduce TSR and GR by up to \$79,377,711 in Tax Year(s) 2022 through 2026.

However, because this provision would start at the beginning of a firm's tax year, they will adjust their declarations. Based on historical revenue information, B&P determined that corporate taxes are received 50% in Fiscal Year 1 and 50% in Fiscal Year 2. Therefore, B&P estimates that this section will reduce TSR and GR by up to \$39,688,856 in Fiscal Year 2022 and Fiscal Year 2027. This section will reduce TSR and GR by up to \$79,377,711 in Fiscal Year 2024 through Fiscal Year 2026. Table 2 shows the estimated impact by fiscal year.

Table 2: Impact by Fiscal Year

Fiscal Year	Loss to GR
FY 2022	(\$39,688,856)
FY 2024	(\$79,377,711)
FY 2024	(\$79,377,711)
FY 2025	(\$79,377,711)
FY 2026	(\$79,377,711)
FY 2027	(\$39,688,856)

Officials from **DOR** state, starting January 1, 2022, and through December 2026, any corporations registered in Missouri with certain NAICS codes would be exempt from owing corporate tax. The following NAICS codes are impacted:

- 332992 – Small Arms Ammunition Manufacturing
- 332994 – Arms, Ordnance, and Ordnance Accessories Manufacturing
- 541715 – Research and Development in the Physical, Engineering, and Life Sciences (except Nanotechnology and Biotechnology)
- 624210 – Community Food Services
- 624410 – Child Day Care Services
- 722511 – Full-Service Restaurants
- 722513 – Limited-Service Restaurants

It should be noted that corporations are not required to provide a NAICS code when registering their corporation in Missouri. Therefore, DOR was unable to determine the number of Missouri corporations that currently may be allowed to claim this corporate tax exemption.

Using information from the US Census Bureau DOR was able to estimate that there are 7,492 businesses with revenues of \$8,448,608,000 that may be eligible for this exemption. It should be noted that many of the community food services providers may be already exempt from tax based on their current structure. Using information on the number of firms that file as corporations, DOR was able to estimate that this could result in a loss to GR by an amount up to \$79,377,711.

Oversight reviewed industry reports the for the NAICS codes that would be impacted by this section. The information reported below are the findings from the industry reports reviewed:

Barnes Reporting					
NAICS CODE	NAICS Title	Number of Establishments in U.S.	Number of Firms in U.S.	Number of Establishments in Missouri	Estimated Number of Firms In Missouri (proportional to number of establishments in Missouri over number of establishments in U.S.)
332992	Small Arms Ammunition Manufacturing	2026	165	143	12
332994	Small Arms Manufacturing	5653	441	106	8
541715	Research and Development in Physical, Engineering, and Life Sciences (except Nanotechnology and Biotechnology)	Unknown	Unknown	Unknown	Unknown
624210	Community Food Services	6462	3452	185	99
624410	Child Day Care Services	428870	61819	8343	1203
722511	Full-Service Restaurants	287535	228094	5106	4050
722513	Limited-Service Restaurants	279558	172786	4808	2972

Oversight notes the industry reports provide the estimated number of firms recognized in the United States, the estimated number of establishments recognized in the United States, and the estimated number of establishments recognized in the State of Missouri.

Oversight notes the industry reports **did not** provide the estimated number of firms recognized in the State of Missouri.

Oversight notes firms may operate one or more establishments and establishments should not be mistaken for the number of business firms operating under each NAICS code.

Oversight has estimated the number of firms that may be recognized in the State of Missouri by applying the proportion of estimated establishments recognized in the United States that are located in Missouri to the estimated number of firms recognized in the United States.

Oversight notes, though, that not all firms are incorporated and; therefore, would not pay Corporate Income Tax. Oversight is unable to estimate the actual and true number of incorporated firms located in Missouri that are included in the NAICS codes that would be impacted by this section. For purposes of this fiscal note, Oversight will report the revenue reduction as a result of this section equal to “less than or greater than” the estimates provided by B&P, beginning in Fiscal Year 2022.

<u>FISCAL IMPACT – State Government</u>	FY 2022 (10 Mo.)	FY 2023	FY 2024	Fully Implemented (FY 2027)
GENERAL REVENUE				
<u>Revenue Reduction – Section 620.1039 – Tax Credit For Qualified Research Expenses p. 7</u>	\$0	Up to (\$10,000,000)	Up to (\$10,000,000)	Up to (\$10,000,000)
<u>Cost – DED – Section 620.1039 – Administration Of Tax Credit p. 4-5</u>				
Personnel Services	(\$42,218)	(\$51,168)	(\$51,679)	(\$53,245)
Fringe Benefits	(\$24,199)	(\$29,209)	(\$29,382)	(\$31,641)
Equipment & Expense	(\$6,242)	(\$2,661)	(\$2,727)	(\$2,937)
Total Cost – DED	(\$72,659)	(\$83,038)	(\$83,788)	(\$87,823)
FTE Change – DED	1 FTE	1 FTE	1 FTE	1 FTE
<u>Cost – DOR – Section 620.1039 – Redemption /Transfer/Error Processing Of Tax Credits p. 4</u>		Up to...	Up to...	Up to...
Personnel Services	\$0	(\$73,811)	(\$74,549)	(\$76,808)
Fringe Benefits	\$0	(\$60,731)	(\$60,980)	(\$61,743)
Equipment & Expense	\$0	(\$31,134)	(\$1,509)	(\$1,626)
Total Cost	\$0	(\$165,676)	(\$137,038)	(\$140,177)
FTE Change – DOR	0 FTE	3 FTE	3 FTE	3 FTE
<u>Revenue Reduction – Section 1 – Exemption From Corporate Income Tax p. 9</u>	<u>Less than or greater than (\$39,688,856)</u>	<u>Less than or greater than (\$79,377,711)</u>	<u>Less than or greater than (\$79,377,711)</u>	<u>Less than or greater than (\$39,688,856)</u>
ESTIMATED NET EFFECT ON	<u>Less than or greater than (\$39,761,515)</u>	<u>Less than or greater than (\$89,626,425)</u>	<u>Less than or greater than (\$89,598,537)</u>	<u>Less than or greater than (\$49,916,856)</u>

GENERAL REVENUE FUND				
-----------------------------	--	--	--	--

<u>FISCAL IMPACT – Local Government</u>	FY 2022 (10 Mo.)	FY 2023	FY 2024	Fully Implemented (FY 2027)
	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>	<u>\$0</u>

FISCAL IMPACT – Small Business

Any small business operating under any of the NAICS codes that would become “exempt” from Corporate Income Tax between Tax Year(s) 2022 through 2026 could positively benefit as such small business would experience increased profit(s) equal to the amount(s) such small business would have otherwise paid in Corporate Income Tax.

FISCAL DESCRIPTION

Currently, no tax credits for qualified research expenses, as defined in the bill, can be approved, awarded, or issued.

Beginning January 1, 2022, the Director of the Department of Economic Development may authorize a taxpayer a tax credit of up to 10% of a taxpayer's additional qualified research expenses, as defined in the bill, or 17% if the additional research expenses relate to research that is conducted in conjunction with a public or private college or university located in this state. However, no tax credit will be allowed for any portion of qualified research expenses that exceed 200% of the taxpayer's average qualified research expenses incurred during the three immediately preceding tax years.

For tax credits that exceed the taxpayer's tax liability, the difference between the credit and the tax liability may be carried forward for 12 years.

Tax credits provided under this program may be transferred, sold, or assigned by filing a notarized endorsement with the Department of Economic Development (DED) that names the transferee, the amount of tax credit transferred, and the value received for the credit, as well as any other information reasonably requested by the DED. For a taxpayer with flow through tax treatment to its members, partners, or shareholders, the tax credit shall be allowed to members,

partners, or shareholders in proportion to their share of ownership on the last day of the taxpayer's tax period.

The annual aggregate cap on the amount of these tax credits that can be authorized by the DED is \$10 million with no single taxpayer being issued or awarded more than \$300,000. Five million dollars of the \$10 million cap in tax credits will be reserved for minority business enterprises, women's business enterprises, and small businesses. Any reserved amount not issued or awarded to a minority business enterprise, women's business enterprise, or small business by November 1st of the tax year may be issued to any taxpayer otherwise eligible for a tax credit under this bill.

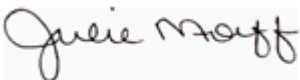
The provisions of the bill that concern a tax credit for qualified research expenses sunsets on December 31st, six years after the effective date of this bill unless reauthorized by the General Assembly. (Section 620.1039, RSMo)

Under this bill, for a period of five years, beginning on January 1, 2022, any corporation registered in Missouri described by NAICS codes 332992; 332994; 541715; 624210; 624410; 722511; or NAICS 722513 will be exempt from the corporate income tax (Section 1).

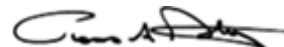
This legislation is not federally mandated, would not duplicate any other program and would not require additional capital improvements or rental space.

SOURCES OF INFORMATION

Office of Administration – Budget & Planning Division
Missouri Department of Commerce and Insurance
Missouri Department of Revenue
Missouri Department of Economic Development



Julie Morff
Director
April 19, 2021



Ross Strobe
Assistant Director
April 19, 2021