



April 10, 2023

SUMMARY OF BILL AS AMENDED (004955, 006724, 007182): Makes various changes to the business tax law, franchise and excise tax law, and sales and use tax law.

Business Tax:

Effective upon becoming law for tax year ending on or after December 31, 2023, increases, from \$50,000 to \$100,000, the minimum threshold of compensation earned from contracts for various types of work in a county or incorporated municipality that requires a business to file a business tax return in that location. Decreases, from three-tenths of one percent to one-tenth of one percent, the business tax rate for industrial loan and thrift companies. Extends the business tax exemption for goods sold from a manufacturing location to any goods sold from a facility within 10 miles of the manufacturing location and extends such exemption to manufacturing locations outside of this state. Increases, from \$10,000 to \$100,000 in gross receipts, the filing threshold for state and local business tax.

Effective April 1, 2024, decreases, from 43 percent to 42.62 percent, the allocation of business tax collections to the General Fund that is made after allocations to county clerks and city officials.

Franchise and Excise Tax:

Adjusts the apportionment formula for determining excise taxes to a single sales factor that will be phased in over a three-year period through December 31, 2025. Requires certain telecommunications companies to continue using the current apportionment formula. Effective upon becoming law for tax year ending on or after December 31, 2023, conforms excise tax law regarding depreciation of certain assets with federal *Tax Cuts and Jobs Act* of 2017 for assets purchased on or after January 1, 2023. Creates a franchise and excise tax credit for tax years ending before December 31, 2025, for employers paying paid family and medical leave. Effective January 1, 2024 establishes a \$50,000 standard excise tax deduction for tax years ending on or after December 31, 2024.

Effective upon becoming law, specifies for the purpose of excise tax law that “certified distribution sales” includes sales of alcoholic beverages when such sales are made in this state to an affiliate that continues the manufacturing process prior to final sale for consumption outside this state.

Effective January 1, 2024, authorizes affiliates of taxpayers to qualify for application of the certified distribution sales election for excise tax purposes.

Effective January 1, 2025, decreases, from 10 percent to 7.5 percent, the receipts factor threshold that a taxpayer must meet, and requires more than 50 percent of the taxpayer's sales in this state to be certified distribution sales for eligibility to apply the certified distribution sales election for excise tax purposes.

Effective upon becoming law for tax years ending on or after December 31, 2024, creates a \$500,000 property exemption for franchise tax. Adjusts the apportionment formula for determining net worth for franchise taxes to a single sales factor that will be phased in over a three-year period through December 31, 2025.

Increases, from 15 to 25 years, the period of time that tax credits earned in tax years ending on or after December 31, 2008 may be carried forward.

Sales and Use Tax:

Creates a sales tax holiday for the retail sale of food and food ingredients sold between 12:01 a.m. on August 1, 2023, and 11:59 p.m. on October 31, 2023.

Effective January 1, 2024, imposes the sales tax on the repair of certain tangible personal property, computer software, laundering and dry-cleaning services, installation of certain personal property, and installation of computer software, when such repair, cleaning, or installation occurs at a place of business outside Tennessee and the property is delivered within the physical limits of this state for use or consumption in this state. Specifies that such services performed within this state but the property is shipped outside this state are not considered sales sourced to this state.

Removes the sales and use tax exemption for magazines and books that are sold to consumers by United States mail or common carrier for certain sellers and cooperative direct mail advertising.

Specifies that the sale of advertising and direct mail that is made from a place of business within this state and delivered to a recipient within this state is sourced to the seller's place of business; exempts such mail from sales tax when being shipped outside of this state. Specifies that the lease or rental of a product that is made from a place of business within this state and delivered to a recipient within this state is sourced to the seller's place of business; exempts such lease or rental from sales tax when the product is delivered outside of this state.

Defines multiple terms related to telecommunications services as it pertains to sales and use tax.

FISCAL IMPACT OF BILL AS AMENDED:

Increase State Revenue – Net Impact – \$19,620,000/FY28-29
\$14,120,000/FY29-30
\$11,460,000/FY30-31
\$8,580,000/FY31-32
\$7,520,000/FY32-33

\$4,960,000/FY33-34

Decrease State Revenue – Net Impact –

\$404,095,500/FY23-24
\$272,885,000/FY24-25
\$163,445,000/FY25-26
\$56,680,000/FY26-27
\$2,540,000/FY27-28
\$2,600,000/FY34-35
\$9,715,000/FY35-36
\$15,815,000/FY36-37
\$18,995,000/FY37-38
\$19,895,000/FY38-39 and Subsequent Years

Decrease Local Revenue – \$3,396,700/FY23-24

\$406,800/FY24-25 and Subsequent Years

Other Fiscal Impact – To the extent that there is a delay in adoption of the new franchise and excise tax provisions upon which calculations are based, as well as a delay in adjusted overall lower estimated payments, the estimated decreases in state revenue in FY23-24 could be lower. However, any such impacts are assumed to be offset by the natural growth in the tax base relative to the actual payments for tax year 2021 that are utilized in the calculations behind these estimates.

The Governor’s proposed budget for FY23-24, on page A-39, recognizes a one-time net decrease in state revenue of \$412,476,800.

Assumptions for the bill as amended:

- The Fiscal Review Committee (FRC) staff does not have access to individual taxpayer information utilized in the calculations of the impacts on business tax and franchise and excise tax revenue. Therefore, the FRC staff cannot independently verify their accuracy.

Business Tax

- According to the Department of Revenue (DOR), based on taxpayer information, increasing, from \$50,000 to \$100,000, the minimum threshold of compensation earned from contracts for various types of work in a county or incorporated municipality that requires a business to file a business tax return in that location will result in a decrease in total business tax collections of \$7,912,000 in FY23-24 and \$9,890,000 in FY24-25 and subsequent years.
- Decreasing the tax rate from three-tenths to one-tenth for industrial loan and thrift companies is estimated to result in a decrease in total business tax revenue of \$244,800 in FY23-24 and \$306,000 in FY24-25 and subsequent years.
- Based on information from DOR, extending the manufacturing exemption to a 10 miles radius and to manufacturing locations outside of this state will result in a decrease in

total business tax revenue of approximately \$1,600,000 in FY23-24 and \$2,000,000 in FY24-25 and subsequent years.

- Changing the apportionment rate of business taxes to the General Fund from 43 percent to 42.62 percent will effectively increase the amount of business tax allocated to local governments.
- The resulting increase in local revenue resulting from this allocation change will equally offset the decrease in business tax allocations due to changes in this legislation; therefore, any net impact on local business tax revenue is estimated to be not significant.

Franchise and Excise Tax

- Phasing in a single sales factor apportionment for franchise and excise taxes will take place as follows for tax years ending:
 - Before December 31, 2024: $\text{Net Earnings} \times [(5 \times \text{Sales}) + \text{Property} + \text{Payroll}] / 7$
 - On or after December 31, 2024, but before December 31, 2025: $\text{Net Earnings} \times [(11 \times \text{Sales}) + \text{Property} + \text{Payroll}] / 13$
 - On or after December 31, 2025: $\text{Net Earnings} \times \text{Sales}$
- Expanding the definition of certified distribution sales will allow certain taxpayers to elect an alternate apportionment.
- According to the DOR, based on taxpayer information, adjusting the apportionment formula to a single sales factor and accounting for the alternate apportionment option will result in an increase in total franchise and excise tax collections of \$16,800,000 in FY23-24, \$91,990,000 in FY24-25, \$186,720,000 in FY25-26, and \$227,725,000 in FY26-27 and subsequent years.
- The current state excise tax rate is 6.5 percent.
- Establishing a standard deduction for excise tax of \$50,000 will result in tax savings of up to \$3,250 ($\$50,000 \times 6.5\%$) per taxpayer.
- This deduction is effective beginning in tax years ending on or after December 31, 2024. Excise taxes are due on April 15th of the year following a business tax year, or if quarterly payments are made, in April, June, September, and January.
- The total recurring decrease in state revenue resulting from the established deduction is estimated to be \$94,500,000.
- Two estimated payments will be made in FY23-24 representing 40 percent of a full year impact; therefore, the decrease in state revenue in FY23-24 is estimated to be \$37,800,000 ($\$94,500,000 \times 40\%$).
- The total recurring decrease in state revenue resulting from the established deduction is estimated to be \$94,500,000 in FY24-25 and subsequent years.
- The current franchise tax rate is 0.25 percent of the greater of net worth or real tangible property in the state.
- Establishing a \$500,000 property exemption for franchise tax will result in tax savings up to \$1,250 per tax payer.
- This exemption is effective beginning in tax years ending on or after December 31, 2023. Franchise taxes are due on April 15th of the year following a business tax year, or if quarterly payments are made, in April, June, September, and January.
- The total recurring decrease in state revenue resulting from the established exemption is estimated to be \$51,000,000.

- Two estimated payments will be made in FY23-24 representing 40 percent of a full year impact; therefore; the decrease in state revenue in FY23-24 is estimated to be \$20,400,000 ($\$51,000,000 \times 40\%$).
- The total recurring decrease in state revenue resulting from the established deduction is estimated to be \$51,000,000 in FY24-25 and subsequent years.
- To the extent that there is a delay in adoption of the new franchise and excise tax provisions upon which calculations are based, as well as a delay in adjusted overall lower estimated payments, the estimated decreases in state revenue in FY23-24 could be lower. However, any such impacts are assumed to be offset by the natural growth in the tax base relative to the actual payments for tax year 2021 that are utilized in the calculations behind these estimates. Year-to-date growth in franchise and excise tax collections through January 2023 is 14.68 percent; the FRC staff estimate for growth in FY23-24, under current law, is 5.35 percent.
- Conforming excise tax law regarding depreciation of certain assets with federal Tax Cuts and Jobs Act of 2017 for assets purchased on or after January 1, 2023 will allow taxpayers to accelerate depreciation on certain assets.
- Accelerating depreciation of assets will shift depreciation to early tax years, thus reducing a taxpayer's liability in earlier years and increasing it in later years.
- While the precise impact is based on multiple unknown variables, based on information provided by DOR, the impact on state revenue is estimated to be as follows: a decrease in state revenue in the following years: \$64,000,000 in FY23-24; \$131,200,000 in FY24-25; \$64,960,000 in FY25-26; and \$11,960,000 in FY26-27; and an increase in state revenue in the following years: \$30,460,000 in FY27-28; \$48,360,000 in FY28-29; \$39,120,000 in FY29-30; \$33,280,000 in FY30-31; \$30,400,000 in FY31-32; \$29,340,000 in FY32-33; \$26,780,000 in FY33-34; \$19,220,000 in FY34-35; \$10,180,000 in FY35-36; \$4,080,000 in FY36-37; and \$900,000 in FY37-38.
- Employers paying paid family and medical leave will be entitled to a franchise and excise tax credit for tax years ending before December 31, 2025.
- Such credits may be carried forward to subsequent years in order for employers to maximize the credit amount; therefore, impacts will extend beyond the initial two years of the pilot credit to FY29-30.
- Benefits for most employers are typically on a calendar year basis. It's assumed that some employers will be incentivized to opt into paid leave for employees beginning in 2024.
- While the number of employers currently offering paid leave that qualifies for the credit and how many employers will opt in as a result of the available credit is unknown; based on information provided by DOR, the decrease in state revenue is estimated to be \$7,320,000 in FY23-24, \$26,940,000 in FY24-25, \$35,660,000 in FY25-26, \$22,900,000 in FY26-27, \$11,180,000 in FY27-28, \$6,920,000 in FY28-29, and \$3,180,000 in FY29-30.
- Based on information provided by DOR, expanding eligibility for the certified distribution sales election will result in an additional 45 taxpayers being eligible for this election.
- Due to the effective dates of this expansion, the impact will be phased in over the first three fiscal years resulting in a decrease in state revenue of \$7,168,575 in FY23-24, \$46,461,384 in FY24-25, and \$89,271,303 in FY25-26 and subsequent years.

- Authorizing tax credits to be carried forward up to 25 years rather than 15 years will result in a recurring decrease in state revenue of approximately \$650,000 in FY23-24 and subsequent years.

Sales Tax Holiday

- The sales tax exemption in the proposed legislation does not apply to sales from a micro market, or vending machine or device.
- August of 2022 and 2021 both had sales tax holidays on food and food ingredients; therefore, complete sales tax collection data on such products is not available.
- September 2020 collections (August sales activity) for the state food sales tax equaled \$46,269,517.
- The food sales tax growth rate for FY21-22, when accounting for the one-week sales tax holiday, is estimated to be approximately 11.25 percent. Accounting for the one-month sales tax holiday in FY22-23, and based on Fiscal Review Committee Staff estimates, the total increase in sales tax collections is estimated to be 8.95 percent.
- September 2022 collections would have been approximately \$56,081,836 ($\$46,269,517 \times 1.1125 \times 1.0895$) in the absence of a sales tax holiday.
- October 2022 collections (September sales activity) for the state food sales tax equaled \$54,220,230.
- November 2022 collections (October sales activity) for the state food sales tax equaled \$56,083,765.
- Assuming a 4.06 percent growth rate in collections in FY23-24 (FRC staff estimates), total state food sales tax collections for September through November 2023 are estimated to be \$173,141,096 [$(\$56,081,836 + \$54,220,230 + \$56,083,765) \times 1.0406$].
- To account for potential shifts in sales from July to August and from November to October, it is assumed there will be a three percent increase from the number given. Therefore, estimated September through November 2023 collections are \$178,335,329 ($\$173,141,096 \times 1.03$).
- The state tax rate on food is 4.0 percent; the average local option sales tax rate is estimated to be 2.5 percent; the effective rate of apportionment to locals is 4.0276 percent.
- Pursuant to Tenn. Code Ann. § 67-6-710(g), local governments will be held harmless from the loss of revenue resulting from the sales tax holiday. However, according to the DOR, such provision does not include the state-shared portion of 4.0276 percent.
- The decrease in state revenue for the tax holiday is estimated to be \$171,152,695 [$\$178,335,329 \times (100\% - 4.0276\%)$].
- The decrease in local revenue from state sales tax apportionment is estimated to be \$7,182,634 ($\$178,335,329 \times 4.0276\%$).
- Locals will be held harmless through distribution of local apportionment sales tax collections from other goods during the period of the sales tax holiday resulting in an additional decrease in state revenue.
- A decrease in state revenue in FY23-24, as a result of holding locals harmless, is estimated to be \$111,459,581 [$(\$178,335,329 / 4\%) \times 2.5\%$] in FY23-24.
- Fifty percent of tax savings will be spent in the economy on other sales-taxable goods and services.

- The amount spent from tax savings on other sales-taxable goods and services from the 2023 tax holiday is estimated to be \$144,897,455 [(\$178,335,329 + \$111,459,581) x 50%].
- The current state sales tax rate is 7.0 percent; the average local option sales tax rate is estimated to be 2.5 percent; the effective rate of apportionment to local government pursuant to the state-shared allocation is estimated to be 3.617 percent.
- The increase in state revenue for the tax holiday is estimated to be \$9,775,956 [(\$144,897,455 x 7.0%) – (\$144,897,455 x 7.0% x 3.617%)].
- The net decrease in local revenue for the tax holiday is estimated to be \$3,193,332 { \$7,182,634 - [(\$144,897,455 x 2.5%) + (\$144,897,455 x 7.0% x 3.617%)] } in FY23-24.
- The total net decrease in state revenue is estimated to be \$272,836,320 (\$171,152,695 + \$111,459,581 - \$9,775,956) in FY23-24.

Other Sales Tax Provisions

Food sales tax collections from micro markets and vending machines are unknown. However, it is assumed that exempting such sales from the proposed food sales tax holiday will not significantly alter the estimated impacts above.

- Any increase in state sales tax revenue on services performed outside of this state will be offset by a decrease in state sales tax revenue from no longer taxing those services when the finished product is delivered outside of this state.
- Any decrease in state sales tax revenue from exempting certain products by no longer considering them sourced in Tennessee will be offset by the removal of other exemptions; the net impact is estimated to be not significant.
- Lease payments for personal property are currently subject to state sales tax, with the exception of a motor vehicle that is removed from the state within three days.
- This legislation will remove this sales tax when the property is delivered outside of this state.
- Based on information from DOR, total lease payments for motor vehicles of approximately \$918,000,000 annually result in approximately \$64,260,000 (\$918,000,000 x 7%) in state sales tax collections.
- Based on U.S. Census Bureau data, about 2.3 percent of residents in Tennessee move to another state annually.
- There will be a decrease in state sales tax collections on leased vehicles of \$1,477,980 (\$64,260,000 x 2.3%) in FY23-24 and subsequent years.
- The total amount of state sales tax collected on other leased items such as equipment, furniture, and other items is unknown. It's reasonably estimated that the total decrease in state sales tax collections will be approximately \$2,000,000.
- The current state sales tax rate is 7.0 percent; the average local option sales tax rate is estimated to be 2.5 percent; the effective rate of apportionment to local government pursuant to the state-shared allocation is estimated to be 3.617 percent.
- A recurring decrease in state sales tax revenue of \$1,927,660 [\$2,000,000 – (\$2,000,000 x 3.617%)].

- Pursuant to Tenn. Code Ann. § 67-6-702, the local option sales tax only applies to the first \$1,600 of any single article, resulting in an effective tax of \$40 per item priced over \$1,600 ($\$1,600 \times 2.5\%$).
- Based on information provided by DOR, approximately 3,700 leased vehicles will be impacted by this legislation, resulting in a recurring decrease in local sales tax revenue of \$148,000 ($\$40 \times 3,700$).
- Sales of all other items are estimated to be \$522,020 ($\$2,000,000 - \$1,477,980$).
- A recurring decrease in local sales tax revenue of \$406,776 $\{[(\$522,020 / 7\%) \times 2.5\%] + (\$2,000,000 \times 3.617\%) + \$148,000\}$.
- Due to the January 1, 2024 effective date, there will be a half year impact in FY23-24.
- The decrease in state revenue will be \$963,830 ($\$1,927,660 \times 50\%$) in FY23-24 and \$1,927,660 in FY24-25 and subsequent years.
- The decrease in local revenue will be \$203,388 ($\$406,776 \times 50\%$) in FY23-24 and \$406,776 in FY24-25 and subsequent years.

Total Impact Assumptions

- The total net decrease in state revenue in FY23-24 is estimated to be \$404,095,505 $[(\$7,912,000 + \$244,800 + \$1,600,000 + \$37,800,000 + \$20,400,000 + \$7,168,575 + \$64,000,000 + \$7,320,000 + \$272,836,320 + \$963,830 + \$650,000) - \$16,800,000 \text{ increase}]$.
- The total net decrease in state revenue in FY24-25 is estimated to be \$272,885,044 $[(\$9,890,000 + \$306,000 + \$2,000,000 + \$94,500,000 + \$51,000,000 + \$46,461,384 + \$131,200,000 + \$26,940,000 + \$1,927,660 + \$650,000) - \$91,990,000 \text{ increase}]$.
- The total net decrease in state revenue in FY25-26 is estimated to be \$163,444,963 $[(\$9,890,000 + \$306,000 + \$2,000,000 + \$94,500,000 + \$51,000,000 + \$89,271,303 + \$64,960,000 + \$35,660,000 + \$1,927,660 + \$650,000) - \$186,720,000 \text{ increase}]$.
- The total net decrease in state revenue in FY26-27 is estimated to be \$56,679,963 $[(\$9,890,000 + \$306,000 + \$2,000,000 + \$94,500,000 + \$51,000,000 + \$89,271,303 + \$11,960,000 + \$22,900,000 + \$1,927,660 + \$650,000) - \$227,725,000]$.
- The total net decrease in state revenue in FY27-28 is estimated to be \$2,539,963 $[(\$9,890,000 + \$306,000 + \$2,000,000 + \$94,500,000 + \$51,000,000 + \$89,271,303 + \$11,180,000 + \$1,927,660 + \$650,000) - (\$227,725,000 + \$30,460,000)]$.
- The total net increase in state revenue in FY28-29 is estimated to be \$19,620,037 $[(\$227,725,000 + \$48,360,000) - (\$9,890,000 + \$306,000 + \$2,000,000 + \$94,500,000 + \$51,000,000 + \$89,271,303 + \$6,920,000 + \$1,927,660 + \$650,000)]$.
- The total net increase in state revenue in FY29-30 is estimated to be \$14,120,037 $[(\$227,725,000 + \$39,120,000) - (\$9,890,000 + \$306,000 + \$2,000,000 + \$94,500,000 + \$51,000,000 + \$89,271,303 + \$3,180,000 + \$1,927,660 + \$650,000)]$.
- The total net increase in state revenue in FY30-31 is estimated to be \$11,460,037 $[(\$227,725,000 + \$33,280,000) - (\$9,890,000 + \$306,000 + \$2,000,000 + \$94,500,000 + \$51,000,000 + \$89,271,303 + \$1,927,660 + \$650,000)]$.
- The total net increase in state revenue in FY31-32 is estimated to be \$8,580,037 $[(\$227,725,000 + \$30,400,000) - (\$9,890,000 + \$306,000 + \$2,000,000 + \$94,500,000 + \$51,000,000 + \$89,271,303 + \$1,927,660 + \$650,000)]$.

- The total net increase in state revenue in FY32-33 is estimated to be \$7,520,037 [(\$227,725,000 + \$29,340,000) - (\$9,890,000 + \$306,000 + \$2,000,000 + \$94,500,000 + \$51,000,000 + \$89,271,303 + \$1,927,660 + \$650,000)].
- The total net increase in state revenue in FY33-34 is estimated to be \$4,960,037 [(\$227,725,000 + \$26,780,000) - (\$9,890,000 + \$306,000 + \$2,000,000 + \$94,500,000 + \$51,000,000 + \$89,271,303 + \$1,927,660 + \$650,000)].
- The total net decrease in state revenue in FY34-35 is estimated to be \$2,599,963 [(\$9,890,000 + \$306,000 + \$2,000,000 + \$94,500,000 + \$51,000,000 + \$89,271,303 + \$1,927,660 + \$650,000) - (\$227,725,000 + \$19,220,000)].
- The total net decrease in state revenue in FY35-36 is estimated to be \$11,639,963 [(\$9,890,000 + \$306,000 + \$2,000,000 + \$94,500,000 + \$51,000,000 + \$89,271,303 + \$1,927,660 + \$650,000) - (\$227,725,000 + \$10,180,000)].
- The total net decrease in state revenue in FY36-37 is estimated to be \$17,739,963 [(\$9,890,000 + \$306,000 + \$2,000,000 + \$94,500,000 + \$51,000,000 + \$89,271,303 + \$1,927,660 + \$650,000) - (\$227,725,000 + \$4,080,000)].
- The total net decrease in state revenue in FY37-38 is estimated to be \$20,919,963 [(\$9,890,000 + \$306,000 + \$2,000,000 + \$94,500,000 + \$51,000,000 + \$89,271,303 + \$1,927,660 + \$650,000) - (\$227,725,000 + \$900,000)].
- The total net decrease in state revenue in FY38-39 and subsequent years is estimated to be \$21,819,963 [(\$9,890,000 + \$306,000 + \$2,000,000 + \$94,500,000 + \$51,000,000 + \$89,271,303 + \$1,927,660 + \$650,000) - \$227,725,000].
- The total net decrease in local revenue is estimated to be \$3,396,720 (\$3,193,332 + \$203,388) in FY23-24 and \$406,776 in FY24-25 and subsequent years.

CERTIFICATION:

The information contained herein is true and correct to the best of my knowledge.



Krista Lee Carsner, Executive Director

/jw