

REVENUE ESTIMATING CONFERENCE

TAX: Corporate Income Tax

ISSUE: Tax Credit for Research and Development

BILL NUMBER(S): HB 577

SPONSOR(S): Representative Plakon

MONTH/YEAR COLLECTION IMPACT BEGINS: July 1, 2009

DATE OF ANALYSIS: February 19, 2009

SECTION 1: NARRATIVE

a. Current Law:

Currently, there is no credit for research and development in Florida's Corporate Income Tax.

b. Proposed Change:

The Bill would create a credit for research and development in Florida's Corporate Income Tax similar to the one provided under s. 41 of the Internal Revenue Code, in the Federal Corporate Income Tax. The credit would be 10 percent of the excess of the current year's qualified research expenses over the average of the four prior years' qualified research expenses. The granting of credits is capped at \$15 million per calendar year. A business may not take more than 50 percent of their remaining tax liability after all other credits are taken. Unused credits may be carried forward for up to 5 years, and may be sold to another taxpayer

If a corporation was not in existence for the duration of the based period, the credit will be reduced by 25 percent for each year the business did not exist during the base period.

This bill is effective for tax years beginning on or after January 1, 2010.

SECTION 2: DESCRIPTION OF DATA AND SOURCES

U.S. DOC, Bureau of Economic Analysis, Research and Development Satellite Account, Table 5.1

http://www.bea.gov/rd/xls/1959_2004_rd_data.xls

Internal Revenue Service SOI Tax Stats- Corporation Research Credit Form 6765- Credit for Increasing Research Activities 2003, 2004, 2005: <http://www.irs.gov/taxstats/article/0,,id=164402,00.html><http://www.irs.gov/taxstats/article/0,,id=164402,00.html>

Department of Revenue, Corporate Income Tax Collections 2004, 2005.

Internal Revenue Service: SOI Tax Stats – Corporation Complete Report – Table 7 Corporation Returns with Net Income, 2003, 2004, 2005: <http://www.irs.gov/taxstats/bustaxstats/article/0,,id=112834,00.html>

The CPA Journal. States' Tax Credits for Company-Financed Research. A Current Comparison. B. Anthony Billings.

<http://www.nysscpa.org/cpajournal/2007/207/essentials/p40.htm>

State of Pennsylvania Report to the Pennsylvania General Assembly on the Research and Development (R&D) Tax Credit, March 14, 2008: http://www.revenue.state.pa.us/revenue/lib/revenue/R&D_08.pdf

SECTION 3: METHODOLOGY (INCLUDE ASSUMPTIONS AND ATTACH DETAILS)

It is expected that the credit will reach the \$15 million cap. This expectation is based on three observations, each of which independently shows that \$15 million annual credit cap would be reasonable met in the foreseeable future.

First, the Bureau of Economic Analysis shows that national research and development spending is currently over \$200 billion and has been growing at an average rate of 6.4 percent from 1984 to 2004. Assuming that the future growth will be 3.2 percent, that only half of the expenditures are from corporations, and that Florida's share is 3.3 percent of the national, Florida would have twice the R&D credits over the cap.

Second, The Internal Revenue publishes the Qualified Research Credits by industry sector. I calculated the percentage of the research and development credits by sector. I used the Florida corporate income tax and federal tax data to calculate Florida's portion of each major industry, leaving an estimate of 1.45 percent of Qualified Research Credits to be proportioned to Florida. The value is grown to meet the cap in order to determine a growth rate of 3 percent would reach the cap.

REVENUE ESTIMATING CONFERENCE

TAX: Corporate Income Tax
ISSUE: Tax Credit for Research and Development
BILL NUMBER(S): HB 577
SPONSOR(S): Representative Plakon
MONTH/YEAR COLLECTION IMPACT BEGINS: July 1, 2009
DATE OF ANALYSIS: February 19, 2009

Finally, a review of other states' experiences with similar credits showed Pennsylvania is very similar to this proposed bill. According to their report, Pennsylvania has a \$40 million cap and would have \$94.7 million in credits if no cap existed. Although Pennsylvania has a larger manufacturing base than Florida, \$94.6 million is over six times the \$15 million cap in Florida.

Again, all three of these analyses demonstrate the \$15 million cap is likely to be met quickly.

The high estimate assumes that all of the credits would be taken during the year. The low estimate assumes that only a fifth of the credits would be taken each year (based on the 5-year carry forward schedule).

SECTION 4: PROPOSED FISCAL IMPACT

State Impact: All Funds	FY 2009-10 Annualized	FY 2009-10 Cash	FY 2010-11 Cash	FY 2011-12 Cash	FY 2012-13 Cash
High	(\$15 Million)	\$0	(\$15 Million)	(\$15 Million)	(\$15 Million)
Middle					
Low	(\$15 Million)	\$0	(\$3 Million)	(\$6 Million)	(\$9 Million)

SECTION 5: CONSENSUS ESTIMATE (ADOPTED 2/20/09) The conference adopted the high estimate.

	FY 2009-10 Annualized	FY 2009-10 Cash	FY 2010-11 Cash	FY 2011-12 Cash	FY 2012-13 Cash
General Revenue	(15.0)	0	(15.0)	(15.0)	(15.0)
State Trust	0	0	0	0	0
Total State Impact	(15.0)	0	(15.0)	(15.0)	(15.0)
Total Local Impact	0	0	0	0	0
Total Impact	(15.0)	0	(15.0)	(15.0)	(15.0)

Research and Development Expenses in United States and Prorated to Florida 2004 - 2011

	United States		Florida Corporate Share (est.)		
	R&D	Avg Prior 4 yr	R&D	Avg Prior 4 yr	Difference
2004	\$200,897	\$192,203	\$3,315	\$3,171	\$143
2005	\$207,369	\$194,037	\$3,422	\$3,202	\$220
2006	\$214,050	\$196,932	\$3,532	\$3,249	\$282
2007	\$220,947	\$203,715	\$3,646	\$3,361	\$284
2008	\$228,065	\$210,816	\$3,763	\$3,478	\$285
2009	\$235,413	\$217,608	\$3,884	\$3,591	\$294
2010	\$242,997	\$224,619	\$4,009	\$3,706	\$303
2011	\$250,826	\$231,855	\$4,139	\$3,826	\$313

Assumptions

Florida's Share = 3.3%

Corporate Share = 50%

*Growth Rate= 3.2%**

**Growth rate is based on half of the average annual growth from 1984 to 2004 of 6.4 percent*

Source: U.S. DOC, BEA, Research and Development Satellite Account, Table 5.1

http://www.bea.gov/rd/xls/1959_2004_rd_data.xls

Total Qualified Research Expenses by Sector

From Federal Form 6765 Excluding Forms 1120S, 1120-REIT, and 1120-RIC

Estimates based on Samples- Amounts are in thousands of dollars

	2003	2004	2005	2003	2004	2005	Mean
All sectors	\$121,502,358	\$116,131,899	\$129,850,954				
Manufacturing	\$88,688,085	\$84,291,352	\$94,638,356	73.0%	72.6%	72.9%	72.8%
Information	\$13,772,515	\$12,931,082	\$14,172,966	11.3%	11.1%	10.9%	11.1%
Professional, scientific and technical services	\$9,229,518	\$10,048,844	\$11,116,902	7.6%	8.7%	8.6%	8.3%
All Other Sectors	\$9,812,240	\$8,860,621	\$9,922,730	8.1%	7.6%	7.6%	7.8%

Florida Proportion of Federal Corporate Income by Sector

	Federal Income Subject to Tax (For Companies with an Income)		Florida Portion of (Positive) Federal Taxable Income		Percent of Federal Income Proportioned to Florida By Sector		
	2004	2005	2004	2005	2004	2005	Mean
Manufacturing	\$292,967,910	\$449,540,561	\$1,830,119	\$3,593,150	0.6%	0.8%	0.7%
Information	\$50,408,058	\$71,598,982	\$703,564	\$2,294,696	1.4%	3.2%	2.3%
Professional, scientific, and technical services	\$13,724,883	\$16,401,790	\$500,942	\$744,392	3.6%	4.5%	4.1%
Other Sectors	\$499,852,336	\$662,891,286	\$22,032,336	\$27,488,699	4.4%	4.1%	4.3%

	Manufacturing	Information	Professional, scientific and technical services	All Other Sectors	Total (All Sectors)
Percent of Qualified Research Expenditure to Sector (Federal)	72.8%	11.1%	8.3%	7.8%	
Percent of Florida Portion of Taxable Income to Federal Taxable Income by Sector	0.7%	2.3%	4.1%	4.3%	
Proportional Percent of Qualified Research Expense Attributable to Florida	0.52%	0.26%	0.34%	0.33%	1.45%
Total Qualified Research Expenses Federal (2005 Return)	\$129,850,954				
Florida Portion	1.45%				
Estimated Florida Qualified Research Expenses (2005 Return)	\$1,877,541				

Maximum Required Growth Rate to Reach Credit Cap

	Growth Rate	Expenditure (\$ Millions)	Average previous 4 years	Ependiture over previous 4 year Average	10 % Credit
2005		\$1,878			
2006	3.20%	\$1,938			
2007	3.10%	\$1,998			
2008	3.00%	\$2,058			
2009	2.92%	\$2,118	\$1,968	\$150	\$15
2010	2.83%	\$2,178	\$2,028	\$150	\$15
2011	2.76%	\$2,238	\$2,088	\$150	\$15
2012	2.68%	\$2,298	\$2,148	\$150	\$15
2013	2.61%	\$2,358	\$2,208	\$150	\$15
2014	2.55%	\$2,418	\$2,268	\$150	\$15
2015	2.48%	\$2,478	\$2,328	\$150	\$15
2016	2.42%	\$2,538	\$2,388	\$150	\$15
2017	2.36%	\$2,598	\$2,448	\$150	\$15
2018	2.31%	\$2,658	\$2,508	\$150	\$15
2019	2.26%	\$2,718	\$2,568	\$150	\$15
2020	2.21%	\$2,778	\$2,628	\$150	\$15
2021	2.16%	\$2,838	\$2,688	\$150	\$15
2022	2.11%	\$2,898	\$2,748	\$150	\$15
2023	2.07%	\$2,958	\$2,808	\$150	\$15
2024	2.03%	\$3,018	\$2,868	\$150	\$15
2025	1.99%	\$3,078	\$2,928	\$150	\$15
2026	1.95%	\$3,138	\$2,988	\$150	\$15

Seven States use a similar method, Colorado, Delaware, Illinois, Maine, Nebraska, Ohio, and Pennsylvania. Of these, Pennsylvania is the most similar to HB577.

Pennsylvania allows a nonrefundable credit of 10% on the excess of the current year's qualified R&D costs over the prior year's research expenses. Beginning July 1, 2006, the credit increases to 20% for small businesses. To receive the credit, companies must submit an application to the state's Department for Qualified Research and Development Expenses showing the amount of expenses incurred. Pennsylvania allows a maximum of \$40 million in credits for all taxpayers, and at least \$8 million of the total is allocated to qualified small businesses. Qualified expenses mirror the IRC section 41(d) definition. Excess credits may be carried forward for up to 15 taxable years.

Source: The CPA Journal. States' Tax Credits for Company-Financed Research
A Current Comparison. B. Anthony Billings.

<http://www.nysscpa.org/cpajournal/2007/207/essentials/p40.htm>

Pennsylvania 2008 Report Reference:

http://www.revenue.state.pa.us/revenue/lib/revenue/R&D_08.pdf