

Department of Finance and Administration

Legislative Impact Statement

Bill: SB362

Bill Subtitle: TO SUNSET CERTAIN TAX INCENTIVES; TO AMEND THE LAW CONCERNING THE SALES AND USE TAX REFUND FOR THE REPAIR AND PARTIAL REPLACEMENT OF MANUFACTURING MACHINERY AND EQUIPMENT; AND TO DECLARE AN EMERGENCY.

Basic Change :

Sponsors: Senators L. Eads, Bledsoe, J. Dismang, J. English, J. Hendren, Hester, Irvin, B. Johnson, Standridge; Representatives Davis, Ballinger, Bentley, Bragg, Coleman, Collins, Dotson, D. Douglas, Gonzales, Holcomb, Maddox, Richmond, Tucker, J. Williams

SB362 would sunset the InvestArk retention tax credit program for Arkansas manufacturers while providing a sales tax exemption for manufacturers on purchases of repair and replacement parts and services for manufacturing machinery and equipment. The proposal would result in a phase-out of revenue costs associated with the InvestArk program while revenues generated on manufacturing repair, replacement, and modification parts and services would be reduced through reduced tax rates to offset the InvestArk program sunset.

Under the InvestArk program, § 15-4-2706(c), a manufacturing company is eligible for a retention sales and use tax credit if certain conditions are met. To participate in the program, a manufacturing company must have been in continuous operation in Arkansas for at least two (2) years and invest a minimum of five million dollars (\$5,000,000) in a project to construct, expand, or modernize a manufacturing facility. The tax credit amount is based on the investment in land, buildings, and equipment and is established at 7% of the eligible project expenditures. The tax credit is used to pay fifty percent (50%) of the taxpayers monthly direct pay sales and use tax liability. The tax credits are earned for a project period covering up to four (4) years with the established tax credits eligible to be carried forward up to five (5) years. Under the bill, the InvestArk program would sunset on July 1, 2017 with no new applicants for the tax credits being accepted. Program participants would continue to earn and use tax credits for projects that are applied for prior to the sunset date.

Under current sales and use tax provisions, §§ 26-52-447 and 26-53-149, the purchase by manufacturers of repair, replacement, and modification parts and services for their existing items of manufacturing machinery and equipment are eligible for a tax refund of one percent (1%) of the six and one-half percent (6.5%) state sales and use tax. Eligible repair, replacement, and modification parts and services are being purchased for manufacturing machinery that is used directly by the manufacturer in producing, fabricating, manufacturing, assembling, processing, finishing, or packaging articles of commerce at their manufacturing facilities in Arkansas. The manufacturing companies claim the refund amount directly on their monthly direct pay tax return by remitting the five and one-half percent (5.5%) net tax due. The proposal would increase the tax refund amount of the six and one-half percent (6.5%) on an annual basis until the refund amount is equal to the full state sales and use tax rate when the purchases would become fully exempt from taxation in Arkansas. DFA will implement a new rebate procedure for Arkansas manufacturers who remit the sales tax on eligible repair, replacement and modification parts and services to their supplier at the time of purchase. Beginning July 1, 2018, the effective net tax rates would be as follows:

- Effective July 1, 2018, the net tax rate would be 4.5%
- Effective July 1, 2019, the net tax rate would be 3.5%
- Effective July 1, 2020, the net tax rate would be 2.5%
- Effective July 1, 2021, the net tax rate would be 1.5%
- Effective July 1, 2022, the rate will be 0.0% and fully exempt from taxation.

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Revenue Impact :

	Anticipated General Revenue Savings from Ending the InvestArk Program	Anticipated General Revenue Cost to Reduce the Tax Rate on Manufacturing Repair Parts	Net Change in General Revenue
	(millions)	(millions)	(millions)
FY2018	\$1.20		\$1.20
FY2019	\$6.50	\$5.82	\$0.68
FY2020	\$11.70	\$11.93	(\$0.23)
FY2021	\$17.10	\$18.47	(\$1.37)
FY2022	\$20.80	\$25.44	(\$4.64)
FY2023	\$24.10	\$36.48	(\$12.38)
FY2024	\$26.40	\$37.27	(\$10.87)
FY2025	\$27.40	\$38.64	(\$11.24)
FY2026	\$27.40	\$40.22	(\$12.62)

Taxpayer Impact :

All Arkansas manufacturers would have reduced sales tax rates on manufacturing repair, replacement, and modification parts and services with full sales tax exemption beginning July 1, 2022.

Resources Required :

No additional resources required.

Time Required :

Adequate time is provided for implementation

Procedural Changes :

DFA will modify electronic tax return filing system to allow rebate claims by Arkansas manufacturers that do not hold direct pay permits.

Other Comments :

None.

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Legal Analysis :

SB362 provides that the retention tax credit found in § 15-4-2706(c) (formerly known as "InvestArk") will sunset on July 1, 2017. No applications for the credit will be accepted after June 30, 2017; however, taxpayers who file applications for the credit on or before June 30, 2017, will still be able to benefit from the credits as currently provided by law.

SB362 provides that increased refunds for major maintenance and improvement projects found in § 15-4-3501 will sunset on July 1, 2022. No applications for such refunds will be accepted on or after June 30, 2022; however, taxpayers who file applications for the increased refund on or before June 30, 2022, will still be able to benefit from the refund as currently provided by law.

SB362 repeals Subchapter 7 of Arkansas Code, Title 26, to remove "InvestArk" credit provisions that existed prior to passage of the Consolidated Incentive Act of 2003, found at Ark. Code Ann. § 15-4-2701 et seq., and to ensure that manufacturers do not mistakenly attempt to claim the benefits of the credit allowed in Subchapter 7.

SB362 clarifies the current procedure for claiming a refund of tax paid for purchases of parts and labor associated with the modification, replacement, or repair of manufacturing machinery and equipment. Specifically, current law requires that a manufacturer claiming the benefit of the refund hold a direct pay or limited direct pay permit with the intent that manufacturers claim the refund on filed returns. However, confusion has arisen as to whether direct pay or limited direct pay permit holders can file verified claims for refund. Current staffing levels within the department would not permit the department to process large numbers of refund claims. Therefore, the bill amends current law to clarify that direct pay and limited direct pay permit holders must self-refund on filed returns.

SB362 also provides another mechanism to claim the benefit of the refund available for tax paid for purchases of parts and labor associated with the modification, replacement, or repair of manufacturing machinery and equipment. Specifically, beginning July 1, 2018, manufacturers who cannot or will not obtain a direct pay or limited direct pay permit, but who hold a sales and use tax permit, may obtain the benefit of the refund by filing a claim for credit or rebate with the Department. This will be accomplished by offsetting the amount of the claimed credit or rebate against the state tax to be remitted on filed sales and use tax returns. If the credit or rebate exceeds the amount of state tax due, the manufacturer will be entitled to a refund of the difference between the amount of the tax owed and the amount of the claimed credit or rebate.

As the refund available for tax paid for purchases of parts and labor associated with the modification, replacement, or repair of manufacturing machinery and equipment must be claimed by self-refunding or self-rebating on filed returns, no interest will accrue or be paid on such refunds. Statutes of limitation under state law will apply to these refunds.