

Department of Finance and Administration

Legislative Impact Statement

Bill: SB561

As Engrossed: 3/27/2019

Bill Subtitle: TO CREATE THE ARKANSAS TAX REFORM ACT OF 2019; AND TO REFORM THE SALES TAX, INCOME TAX, PROPERTY TAX, AND FRANCHISE TAX LAWS OF THE STATE.

Basic Change :

Sponsors: Sen. J. Hendren and Rep. Dotson

Engrossed 03/27/19 --- House Amendment 1 --- Amends the bill to change the effective date of the transfer of the administration and collection of the Arkansas franchise tax to the Department of Finance and Administration to be effective on May 1, 2021.

Engrossed 03/19/19 --- Senate Amendment 1 --- In reference to the mandatory guidelines to be created by the Assessment Coordination Department, the amendment provides that if a county is found not to be compliant with the guidelines, the Legislative Council or, if the General Assembly is in session, the Joint Budget Committee, may recommend to the General Assembly that that the noncompliant county's funds from the Property Tax Relief Trust Fund to be used by the county assessor for the costs of administering Arkansas Constitution, Amendment 79 may be reduced or withheld until the county becomes compliant.

Original Bill --- SB561 would create the Arkansas Tax Reform Act of 2019 to reform the tax laws of the state. The bill would amend provisions of the Arkansas Corporate Franchise Tax, require the Department of Finance and Administration (DFA) to provide reports on tax exemptions and deductions, require the Assessment Coordination Department to establish certain guidelines, to provide sales tax exemptions, and to provide procedures to regulate the sales tax farm exemption as it relates to the sale of ATVs.

Franchise Tax --- the bill amends various provisions of Arkansas Code regarding the Arkansas Franchise tax remitted by corporations. The bill also transfers administration and collection of the Arkansas franchise tax from the Arkansas Secretary of State to the Department of Finance and Administration (DFA). This transfer of responsibility would be effective on January 1, 2020.

Property Tax --- Requires the Assessment Coordination Department (ACD) to adopt mandatory guidelines to be followed by County Assessors with regard to identifying property exempt from ad valorem tax and for assessing business inventory. Once implemented, these guidelines are to be followed by County Assessors and ACD is to monitor each county's compliance and report any non-complaint county to the General Assembly.

Report of Tax Exemptions and Deductions --- Provides that before each regular session of the General Assembly, DFA shall report to the Legislative Council and the Governor on the effect of each tax exemption, discount, credit and deduction relating to state income tax and state sales and use tax. If actual tax return data is not available, DFA would use statistical data to make an estimate. If the information cannot be determined, an explanation must be provided. The required report would include:

- An estimate of the loss of revenue for a six-year period beginning with the fiscal year in which the report is submitted;
- A citation to the legal authority for the exemption, discount, exclusion, credit, deduction, special accounting treatment, or special rate; and

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- For an exemption, discount, credit or deduction, that reduces revenue by more than one percent (1%) of the total revenue for the relevant tax, the effect of the distribution of the tax burden by income class; and industry or business class.

The report may include an assessment of the intended purpose of the tax provision and a recommendation for retaining the provision.

Sales Tax --- Advertising Space --- The bill would amend existing law to provide a sales tax exemption for advertising space placed on a public transit bus. This provision of the bill would be effective the first day of the calendar quarter following the effective date of the act. (October 1, 2019).

Sales Tax --- All Terrain Vehicles --- Amends provisions of the existing sales tax exemption on the purchase of certain types of farm machinery and equipment to provide that to the extent that the farm machinery exemption applies to an all-terrain vehicle, additional information will be required at the time of purchase to provide additional identifying information regarding eligibility for the exemption. DFA would develop forms for use in supplying the information and would include the following:

- The purchaser's person's name and contact information;
- The purchaser's tax identification number;
- The make, model, year, and identification number of the all-terrain vehicle;
- A signed statement indicating that the person understands that the use of an exemption for the purchase of an all-terrain vehicle may be subject to audit by DFA; and
- Any other information required by DFA to aid in the administration of the tax exemption.

The seller of the all-terrain vehicle would submit the completed forms to DFA at the time of filing their monthly sales tax return allowing DFA to review and audit unauthorized exemption claims. This provision of the bill would be effective the first day of the calendar quarter following the effective date of the act. (October 1, 2019).

Revenue Impact :

-\$50,000 Total Annual Loss to State Revenues --- Transit Advertising Services

- -\$33,542 --- State General Revenue (4.5%)
- -\$6,522 --- Educational Adequacy (.875% tax)
- -\$3,727 --- Property Tax Relief Trust Fund (.5%)
- -\$932 --- Conservation Tax (.125%)
- -\$3,727 --- Highway Fund (.5%)
- -\$1,050 --- State Central Services
- -\$500 --- Constitutional Officers

City and County Sales Tax Loss --- \$16,700

Taxpayer Impact :

Sellers of all-terrain vehicles would submit on a monthly basis exemption claim forms completed by the ATV purchaser when claiming a farm machinery exemption on the ATV purchase. Corporations would

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work with both DFA and the office of Arkansas Secretary of State during the annual renewal processes and payment of the franchise tax.

Resources Required :

Report of Tax Exemptions and Deductions --- \$875,000 Additional DFA staff personnel and consultant services will be needed to prepare the biennial reports of the economic impact from income tax and sales and use taxes exemptions, deductions, exclusions, etc. The dedicated staffing that would be needed to compile the necessary information on a fiscal year basis are the following: hiring of one economist and one statistician and one administrative assistant, \$250,000 per year; consultant services, computer software services, etc. Initially, one additional DFA Tax Research Analyst, A057C position will be needed.

Franchise Tax - Initial Year \$2.7 Million; Subsequent Annual Cost \$675,000

Initial Year of Implementation --- Computer programming, forms and instructions modification, Initial Implementation \$2.3 Million. Printing and mailing of forms \$100,000 per year. DFA's Corporation Income Tax Section would need two additional supervisors, five taxpayer service representatives and two new auditors to process and review both combined Income and Franchise Tax as well as stand-alone Franchise Tax returns at a cost of \$287,000 per year.

Subsequent Annual Cost --- Computer programming, forms and instructions modification, annual system maintenance \$288,000 per year. Annual printing and mailing of forms \$100,000 per year. Ongoing personnel costs of \$287,000 per year.

Income Tax Processing may need additional imaging equipment and additional data entry personnel. Training for Secretary of State, Corporation Income Tax, Individual Income Tax, Field Audit, AIRS, Data Processing, Revenue Legal Counsel and others to administer the new tax.

Time Required :

Adequate time is provided for implementation.

Procedural Changes :

Report of Tax Exemptions and Deductions - Development of new procedures to implement creation of biennial reports of tax exemptions, discount, exclusion, credit, etc. No current requirement for this type of information is required of DFA and data sources available for this type of reporting is limited from the tax return records maintained. U.S. Economic Census data in conjunction to any private and public reports and publications are generally used in revenue and exemption estimating by DFA for tax purposes. When used, U.S. Economic Census data must be factored to reflect the Arkansas portion based on population and income levels. U.S. Economic data is updated on a five-year cycle which would not correspond to the biennial nature of the proposal.

ATVs --- Notification to farm implement and all-terrain vehicle dealers of the change in process and instructions for submission of required data.

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Franchise Tax --- In addition to the hiring of more personnel, existing employees would need additional training on franchise tax requirements and processing.

Other Comments :

Report of Tax Exemptions and Deductions --- The Department does not currently have access to some of the data necessary to provide biennial updates of exemptions, discount, credits and deductions. U.S Economic Census data is updated on five-year cycles with only a portion updated and completed each year.

Legal Analysis :

The bill amends various provisions of state tax law as discussed below.

Franchise Tax --- The bill transfers administration of the Arkansas franchise tax from the Secretary of State to DFA and amends state law as needed to accomplish that transfer. Additional instructions regarding the waiver of past due franchise tax penalty and interest have been added. This transfer is effective on and after May 1, 2021. The bill provides that DFA may adopt rules to implement and administer the franchise tax.

Property Tax --- The bill requires the Assessment Coordination Department (ACD) to adopt mandatory guidelines for county assessors to follow regarding the identification of property exempt from ad valorem tax and the assessment of business inventory. Once implemented, these guidelines are to be followed by county assessors and ACD is to monitor each county's compliance. Non-complaint counties are to be reported by ACD to the General Assembly.

Administrative Provisions --- The bill requires DFA to file a biennial report with the General Assembly prior to each regular session reporting the effect of each state income tax and sales and use tax exemption, discount, credit, and deduction.

Sales Tax --- The bill provides that the sale of advertising space on a public transit bus is exempt from sales tax. Additionally, the bill provides that a person claiming the farm machinery sales tax exemption for the purchase of an all-terrain vehicle is required to complete a form indicating the person's name and contact information, the person's tax identification number, information regarding the all-terrain vehicle, a statement that the purchaser understands that the transaction may be subject to audit, and other information required by DFA. The retailer selling the all-terrain vehicle is required to forward the completed forms to DFA each month.

Effective Dates --- The bill's provisions related to franchise tax, property tax, and biennial reporting by DFA are effective on and after May 1, 2021. Rules related to these provisions are to be finalized on or before May 1, 2021. The provisions related to sales tax exemptions for advertising space on buses and for all-terrain vehicles are effective on an after the first day of a calendar month following the effective date of the act.