SUMMARY OF PROPOSAL #4
for consideration by the
ARKANSAS TAX REFORM AND RELIEF LEGISLATIVE TASK FORCE

TOPIC: Tax Deduction or Tax Credit to Offset the Arkansas Corporate Franchise Tax

Summary of Proposal for Consideration

To implement a tax deduction or tax credit to be taken against Arkansas individual income tax liability or corporate income tax liability to offset payments made under the Arkansas corporate franchise tax, Arkansas Code § 26-54-101 et seq., effective for tax years beginning January 1, 2019.

Fiscal Analysis

According to the Arkansas Secretary of State, the following chart provides an overview of the corporate franchise tax collections since 2009:[1]

2009 - $22.8 million	2012 - $23.1 million	2015 - $26.3 million
2010 - $24.0 million	2013 - $26.5 million	2016 - $25.6 million
2011 - $23.2 million	2014 - $25.8 million	2017 - $26.1 million

Under Arkansas Code § 26-54-113(b), the first eight million dollars ($8,000,000) of revenues collected under the corporate franchise tax are deposited into general revenues, and the remaining revenues are deposited to the credit of the Educational Adequacy Trust Fund.

According to the Arkansas Secretary of State, it is anticipated that collections from the franchise tax will exceed thirty million dollars ($30,000,000) in fiscal year 2018. According to the Department of Finance and Administration (DFA), depending on the nature of a tax credit or deduction to offset the ad valorem personal property tax paid on business inventory, such a tax credit or deduction may result in an estimated loss of general revenues of approximately thirty million dollars ($30,000,000), based on the Secretary of State's estimated revenue amounts for fiscal year 2018.

Legal Analysis

Background

Arkansas does not currently provide a tax credit or deduction against Arkansas individual income tax liability or corporate income tax liability to offset payments made under the Arkansas corporate franchise tax. However, under Arkansas Code § 26-51-416, Arkansas allows a deduction from income tax for franchise taxes paid by the taxpayer. The deduction was created by ACT 118 of 1929 and has not been amended since.

[1] Source: Arkansas Secretary of State: https://www.sos.arkansas.gov/business-commercial-services-bcs/franchise-tax/

Potential Legal Issues

None.

Other States

- Iowa: Iowa imposes a franchise tax on financial institutions for the privilege of doing business in Iowa, regardless of how the financial institution is treated under federal law. (IA St. §§ 422.60(1), § 422.61(3)(g), and Iowa Admin. Code § 701-59.21). If the financial institution pays individual income tax or corporate income tax, the financial institution may receive a credit against the tax liability of the financial institution for individual income tax or corporate income tax on the amount the institution paid under the franchise tax. (IA St. §§ 422.11 and 422.33(8)). The franchise tax can also be reduced by several tax credits, including without limitation the alternative minimum tax credit, the historic preservation and cultural and entertainment district tax credit, the investment tax credit, the endow Iowa tax credit, the wind energy production and renewable energy tax credit, the Iowa fund of funds tax credit, and the redevelopment tax credit. (IA St. § 422.60).

- Louisiana: Louisiana imposes a franchise tax on every domestic and foreign corporation conducting business in Louisiana. (LA St. § 47:601). Louisiana provides a deduction on corporate and individual income tax for taxes paid under the franchise tax. (LA St. § 47:55). Louisiana also provides several tax credits that may be used to offset tax liability under the franchise tax, including without limitation the Atchafalaya trace tax credit, the previously unemployed tax credit, the recycling tax credit, the basic skills training tax credit, the inventory tax credit, and the research and development tax credit. (LA St. §§ 25:1226.4, 47:6004, 47:6005, 47:6006, 47:6009, and 47:6015).

- Mississippi: Mississippi imposes a franchise tax on corporations for the privilege of doing business in the State of Mississippi. Mississippi's franchise tax is due annually as long as the corporation remains incorporated, domesticated, or continues to do business in Mississippi. (MS St. §§ 27-13-5 and 27-13-7). Mississippi does not provide a credit for the franchise tax. However, Mississippi allows for an income tax deduction taxes for paid under the franchise tax. (MS St. § 27-7-17).

- Missouri: Missouri repealed its corporate franchise tax beginning on January 1, 2016. (MO St. § 147.010(5)).

- Oklahoma: Oklahoma imposes an annual corporate franchise tax on all corporations that do business in Oklahoma. (68 OK St. § 1201). Oklahoma does not provide a credit or deduction for taxes paid under the franchise tax.

- Tennessee: Tennessee imposes a franchise tax on any person, taxpayer, or corporate franchise doing business in Tennessee and having a substantial nexus in Tennessee. Examples of a substantial nexus in Tennessee, include without limitation maintaining an office in the state, regularly selling products and or services in the state, and owning or leasing property located in the state. (TN St. §§ 67-4-2104 and § 67-4-2105). Tennessee also provides several tax credits against franchise tax liability, including without limitation:

    - A tax credit on the purchase price of industrial machinery, where the percentage of the tax credit is based on the amount of capital investment made by the company;
    - A job tax credit, including an additional enhanced job tax credit, for businesses meeting certain requirements where the credit is equal to four thousand five hundred dollars ($4,500) for each qualified job created during the investment period;
    - A job tax credit for employees with disabilities, where the credit is five thousand dollars ($5,000) for each full-time employee and two thousand dollars ($2,000) for each part-time employee;
    - A credit on a portion of a qualified headquarters facility's relocation expenses and investments;
    - A credit for a financial institution that makes investments to an eligible housing entity;
    - A credit for a qualified taxpayer that has established its international, national, or regional headquarters in the state; and
    - A credit on fifteen percent (15%) of the qualified expenses incurred by a qualified production company that has established a headquarters facility in Tennessee.

  (TN St. §§ 67-4-2009 and 67-4-2109).

  Tennessee does not impose a corporate income tax and levies a limited individual income tax only on interest and dividend income, so there are no individual or corporate income tax credits or deductions offered for franchise taxes paid.

- Texas: Texas imposes a franchise tax on entities formed in Texas or doing business in Texas. (TX St. Tax Code § 171.001). Texas also provides three (3) tax credits against the franchise tax:

    - A tax credit for a clean energy project to provide a tax credit equal to the lesser of either ten percent (10%) of the total capital cost of the project or one hundred million dollars ($100,000,000) (TX ST. Tax Code § 171.602);
    - A tax credit for certain research and development activities based on a certain percentage depending on the nature of the research or development activities. The default rate is a credit that equals five percent (5%) on the difference between qualified research expenses incurred by the entity and fifty percent (50%) of the average amount of qualified research expenses incurred during the three (3) preceding tax years. However, alternative rates

are applicable to different types of research and development activities (TX ST. Tax Code § 171.654); and

- A tax credit for rehabilitation of certified historic structures up to twenty-five percent (25%) of the total eligible costs and expenses incurred in the rehabilitation of a certified historic structure. (TX ST. Tax Code § 171.905).

Texas does not impose an individual income tax or corporate income tax, so there are no individual or corporate income tax credits or deductions offered for franchise taxes paid.