

The Florida Senate
BILL ANALYSIS AND FISCAL IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: The Professional Staff of the Committee on Appropriations

BILL: PCS/SB 502 (383058)

INTRODUCER: Appropriations Committee (Recommended by Appropriations Subcommittee on Finance and Tax); and Senator Stargel

SUBJECT: Corporate Income Tax

DATE: February 26, 2018 REVISED: _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	<u>Babin</u>	<u>Diez-Arguelles</u>	<u>AFT</u>	Recommend: Fav/CS
2.	<u>Babin</u>	<u>Hansen</u>	<u>AP</u>	Pre-meeting

Please see Section IX. for Additional Information:

COMMITTEE SUBSTITUTE - Substantial Changes

I. Summary:

PCS/SB 502 updates Florida's corporate income tax by adopting the federal Internal Revenue Code in effect on January 1, 2018. By adopting the updated code, Florida recognizes the changes made to the code. A number of the changes made to the federal code will affect Florida's corporate tax collections.

The bill does not adopt the increased first-year depreciation (bonus depreciation) provisions included in the Tax Cuts and Jobs Act of 2017. Florida corporations must add back those deductions for Florida purposes and then spread the deduction over a seven-year period.

The bill requires the Department of Revenue to establish a workgroup to analyze the effects of the recent federal legislation on the Florida Corporate Income Tax. The workgroup is required to file a report with the Legislature by February 1, 2019.

The bill takes effect upon becoming law and operates retroactively to January 1, 2018.

The Revenue Estimating Conference has determined that the bill has an indeterminate fiscal impact on the General Revenue Fund in Fiscal Years 2017-2018 and 2018-2019, and an indeterminate but positive recurring impact thereafter.

II. Present Situation:

Annual Adoption of the Internal Revenue Code

Florida imposes a 5.5 percent tax on the taxable income of corporations and financial institutions doing business in Florida.¹ A corporation calculates its taxable income for Florida tax purposes by starting with its taxable income determined for federal tax purposes.² Additional adjustments are then made to determine the corporation's Florida taxable income. By starting with federal taxable income, Florida eases the administrative burden on Florida taxpayers.

Florida maintains its relationship with the federal Internal Revenue Code each year by adopting the federal Internal Revenue Code as it exists on January 1 of the year. By doing this, Florida adopts any changes that were made in the previous year to the determination of federal taxable income.

Because Florida relies on federal taxable income to determine Florida taxable income, changes to the calculation of federal taxable income will affect the calculation of Florida taxable income and may increase or decrease Florida tax receipts if Florida adopts the most recent federal Internal Revenue Code. In some instances, Florida has adopted the new federal Internal Revenue Code, but excluded some changes.

The Tax Cuts and Jobs Act of 2017

On December 22, 2017, President Trump signed into law the Tax Cuts and Jobs Act of 2017 (TCJA).³ The TCJA made significant changes to federal income tax provisions related to individuals, corporations, and the treatment of foreign income.

Individual Tax Reforms

The TCJA's changes to the taxation of individual income do not affect Florida tax revenues, as Florida does not have an individual income tax.

Business Tax Reforms

The TCJA's changes to corporate taxes generally:

- Reduce the federal income tax rate on corporate income.⁴
- Significantly increase the first-year deductions related to equipment purchases (bonus depreciation).
- Limit or require amortization of certain business expenses.
- Repeal or curtail certain tax credits and deductions.

¹ Sections 220.11(2) and 220.63(2), F.S.

² See generally s. 220.13(2), F.S.

³ Pub. Law No. 115-97 (December 22, 2017)

⁴ Changes to the federal income tax rate do not directly affect Florida corporate income tax receipts.

The TCJA provides 100 percent bonus depreciation through 2023 and then phases down the percentage to 80 percent, 60 percent, 40 percent, and 20 percent, for the next four years, respectively. No bonus depreciation is granted after 2027.⁵

Bonus depreciation merely affects the timing of depreciation deductions. Under a normal depreciation schedule, deductions are spread over a given time period. Bonus depreciation increases the first-year depreciation amount and thereby decreases out-year depreciation amounts. With 100 percent bonus depreciation, all of the years' depreciation deductions are accelerated into the first year.

International Tax Reforms

The U.S. has historically deferred taxation of foreign-source income until the income was repatriated to the U.S.⁶ The TCJA aims to largely eliminate this deferral for corporations.

The TCJA's foreign income changes generally:

- Require taxation of foreign-source income.
- Provide deductions for certain dividends from foreign corporations.
- Provide temporary, partial credits for certain foreign income to reduce the near-term taxation of that income.

Bipartisan Budget Act of 2018

On February 9, 2018, President Trump signed into law the Bipartisan Budget Act of 2018 (the BBA).⁷ Included within the BBA, Congress reauthorized for a limited time several tax provisions.⁸ These provisions have come to be known as "tax extenders" because Congress has been regularly extending them for brief periods of 1 or 2 years.

The major changes affecting corporate taxes will:

- Accelerate the depreciation of certain assets.
- Increase the first-year expensing of certain film and television production expenses.
- Increase deductions for corporations with manufacturing activities in Puerto Rico.
- Increase deductions for energy efficient commercial building expenses.
- Delay recognition of certain income related to dispositions of utility property.

III. Effect of Proposed Changes:

This bill updates Florida's corporate income tax by adopting the federal Internal Revenue Code in effect on January 1, 2018. By adopting the updated code, Florida recognizes the changes made to the code. A number of the changes made to the federal code will affect Florida's corporate tax collections.

⁵ TCJA, s. 13201

⁶Tax Policy Center, *Briefing Book, Key Elements of the U.S. Tax System*, available at <http://www.taxpolicycenter.org/briefing-book/how-does-current-system-international-taxation-work> (last visited Feb. 17, 2018).

⁷ Pub. Law No. 115-123 (February 9, 2018)

⁸ See BBA, ss. 40101 - 40501

The Tax Cuts and Jobs Act of 2017

Business Tax Reforms

Many of the TCJA's changes to the taxation of corporate income directly affect Florida corporate income tax receipts to the extent that Florida does not "decouple"⁹ from the changes. The effect of each change made by the TCJA varies – some decrease tax receipts, while others increase tax receipts; however, the extent that each change will affect Florida corporate income tax receipts depends upon the specific change and the nature of the corporations involved. For instance, changes that affect manufacturing corporations may not affect Florida as much as states with significant manufacturing activities

The bill decouples from the bonus depreciation provisions included in the TCJA. Florida corporations that claim bonus depreciation on their federal returns must add back that deduction for Florida purposes and then spread the deduction over a seven-year period. This treatment has been used for similar federal provisions over the past several years.¹⁰

International Tax Reforms

The TCJA's changes related to the taxation of corporations' foreign income will likely affect Florida corporate income tax receipts, but the magnitude of the impact on tax receipts cannot be determined at this time. Like most states, Florida excludes (subtracts) certain types of foreign income from its corporate taxable income. At this time, it is unclear if the "new" taxable foreign income and related deductions will be included within those subtractions. Over the coming months, many of those decisions are expected to be made by the Internal Revenue Service.

Bipartisan Budget Act of 2018

Some of the tax extender provisions affect federal taxable income, and thus, these provisions will likely affect the Florida taxable income of affected Florida corporations.

Workgroup to Review the Effects of the Federal Legislation on Florida Corporate Income Tax

The bill provides that the Legislature recognizes that the TCJA will have significant effects on the Florida's corporate income tax and finds that it is necessary to establish a workgroup to better understand the effects. The bill requires the Department of Revenue to establish a workgroup to examine how the implementation for the TCJA will affect state corporate income tax.

⁹ "Decoupling" is the term used to describe a situation when the state adopts the Internal Revenue Code, but does not adopt certain, specific changes to the code. In doing so, the state is said to have "decoupled" from those specific changes. Florida has decoupled from several changes over the past decade, most often with extraordinary first-year depreciation deductions granted at the federal level. The relevant acts were the Economic Stimulus Act of 2008, the American Recovery and Reinvestment Act of 2009, the Small Business Jobs Act of 2010, the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, the American Taxpayer Relief Act of 2012, the Tax Increase Prevention Act of 2014, and The Consolidated Appropriations Act, 2016.

¹⁰ See chapters 2009-192, 2011-229, 2013-46, 2015-35, and s. 14, 2016-220, Laws of Fla.

The workgroup consists of department employees who have expertise in state and federal corporate income tax. The workgroup must consult with the Revenue Estimating Conference and also must seek and consider comments from the private sector.

By February 1, 2019, the workgroup must submit a report to the Governor, President of the Senate, Speaker of the House of Representatives, and the respective chairs of the appropriate legislative committees. The report must include: a comprehensive discussion of issues having an effect on the state corporate tax structure and corporate tax revenues; options for changes to state tax law needed to integrate state law with federal law; the fiscal impact of each option; and whether the workgroup should be extended.

The workgroup is required to submit status reports to the chairs of the appropriate legislative committees on May 15, 2018, July 15, 2018, September 15, 2018, and November 15, 2018. The status reports must include a brief description of the workgroup's activities and any relevant guidance issued by the Internal Revenue Service.

The bill applies retroactively to January 1, 2018.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

The mandate restrictions do not apply because the bill does not require counties or municipalities to spend funds, reduce counties' or municipalities' ability to raise revenue, or reduce the percentage of state tax shared with counties and municipalities.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Fiscal Impact Statement:

A. Tax/Fee Issues:

The Revenue Estimating Conference has determined that the bill has an indeterminate fiscal impact on the General Revenue Fund in Fiscal Years 2017-2018 and 2018-2019, and an indeterminate but positive recurring impact thereafter.

B. Private Sector Impact:

By adopting recent changes to the Internal Revenue Code, Florida provides consistent tax treatment for Florida corporate taxpayers. The effect on an individual corporation will depend on many factors, including the type of activity it conducts. As a group,

corporations will likely pay less tax in Fiscal Years 2017-2018 and 2018-2019 and more taxes in Fiscal Year 2020-2021 and thereafter.

C. **Government Sector Impact:**

None.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Statutes Affected:

This bill substantially amends section 220.03 of the Florida Statutes.

IX. Additional Information:

A. **Committee Substitute – Statement of Changes:**

(Summarizing differences between the Committee Substitute and the prior version of the bill.)

Recommended CS by Appropriations Subcommittee on Finance and Tax on February 20, 2018:

The committee substitute:

- Requires Florida taxpayers to add back amounts taken as bonus depreciation and spread the deduction over a seven-year period.
- Requires the Department of Revenue to establish a workgroup to analyze the effects of the TCJA on state corporate income tax.

B. **Amendments:**

None.