

HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: HB 459

Corporate Income Tax

SPONSOR(S): Cannon

TIED BILLS:

IDEN./SIM. BILLS:

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR
1) Finance & Tax Council		Diez-Arguelles	Langston
2) Policy Council			
3)			
4)			
5)			

SUMMARY ANALYSIS

Florida imposes a 5.5% tax on the taxable income of corporations doing business in Florida. For simplicity's sake, the determination of taxable income for Florida tax purposes begins with the taxable income used for Federal income tax purposes. This means that a corporation paying taxes in Florida receives the same benefits from deductions allowed in determining its federal taxable income.

Florida maintains this relationship by each year 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. The bill adopting the federal code is referred to as the "piggyback bill."

In 2008, due to budgetary constraints, the Legislature adopted the federal tax code, except for two provisions dealing with 50% bonus depreciation and an increased first-year expensing amount. HB 5065 (Ch. 2008-206, L.O.F.) The method chosen to exclude the benefit of the federal provisions from the Florida corporate income tax calculations was to provide an addition to a corporation's Florida taxable income equal to the amount deducted from the federal tax return because of the two provisions.

Because of the interaction of the federal tax code with the Florida tax code, the adopted method placed a taxpayer choosing to take advantage of the federal provisions in a worse position for Florida tax purposes than it would have been had it not taken advantage of the federal provisions. This was not the result the legislature intended. The intent was that Florida tax liability should not be affected by a taxpayer's choice regarding the two federal provisions.

This bill replaces the statutory changes made last year with a new procedure to account for bonus depreciation and additional expensing in a way that will largely correct the negative financial effects of HB 5065 on Florida taxpayers. Specifically, the bill spreads out the amount of bonus depreciation or additional expensing claimed by a taxpayer on the federal return over a 5-year period on the Florida return. The bill accomplishes this by providing that a taxpayer claiming bonus depreciation or additional expensing on its federal return must add 80% of the amount so claimed to Florida taxable income. In each of the 4 subsequent taxable years, the taxpayer can subtract from taxable income 25 percent of the amount by which taxable income was increased. These changes will approximate the depreciation allowances that would have occurred absent the two federal provisions.

The bill has an indeterminate fiscal impact on state government revenues.

The bill has an effective date of upon becoming law and applies retroactively to January 1, 2008.

HOUSE PRINCIPLES

Members are encouraged to evaluate proposed legislation in light of the following guiding principles of the House of Representatives

- Balance the state budget.
- Create a legal and regulatory environment that fosters economic growth and job creation.
- Lower the tax burden on families and businesses.
- Reverse or restrain the growth of government.
- Promote public safety.
- Promote educational accountability, excellence, and choice.
- Foster respect for the family and for innocent human life.
- Protect Florida's natural beauty.

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. EFFECT OF PROPOSED CHANGES:

CURRENT LAW

Corporate Income Tax Overview

Florida imposes a 5.5% tax on the taxable income of corporations doing business in Florida.¹ For simplicity's sake, the determination of taxable income for Florida tax purposes begins with the taxable income used for Federal income tax purposes.² This means that a corporation paying taxes in Florida receives the same benefits from deductions allowed in determining its federal taxable income. With federal taxable income as a starting point, Florida law then requires a variety of additions and subtractions to reflect Florida-specific policies.

Florida maintains this relationship by each year 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. The bill adopting the federal code is referred to as the "piggyback bill."

Depreciation Deduction

Under federal tax law, a corporation is entitled to reduce its income over time to reflect the cost of an asset it purchases. If a corporation purchases equipment for \$10,000 with an expected useful life of 5 years, it is entitled to reduce its income by annual amounts totaling \$10,000 over 5 years. For example, if the corporation uses the straight-line depreciation method, it can reduce its income by \$2,000 each year for 5 years.

Under Florida law, this treatment for federal tax purposes flows to the Florida tax return and reduces Florida taxable income.

Economic Stimulus Act of 2008 and Florida's Response

In early 2008, Congress approved the Economic Stimulus Act of 2008. Among other items, this legislation provided two tax benefits to corporations: (1) it allowed corporations to take an additional depreciation deduction equal to 50% of the cost of property placed in service in 2008, and (2) it allowed for small businesses to completely depreciate property valued up to \$250,000 (instead of \$128,000)

¹ Sec. 220.11, F.S.

² Secs. 220.12 and 220.13, F.S.

placed in service during 2008. The effect of these changes was to increase depreciation and expensing provisions in the year property is placed in service and to decrease depreciation deductions in later years.

On February 22, 2008, the Revenue Estimating Conference determined that if Florida adopted the federal code, including the two provisions, state revenues would decline by \$146.8 million in FY 08-09 and by \$76 million in FY 09-10. The decline would be offset in later years when revenues would be higher than otherwise.

Due to budgetary constraints in FY 08-09, the Legislature decided to adopt the federal tax code, except for the provisions dealing with 50% bonus depreciation and the increased expensing amount. HB 5065 (Ch. 2008-206, L.O.F.) The method chosen to exclude the benefit of the federal provisions from the Florida corporate income tax calculations was to provide an addition to a corporation's Florida taxable income equal to the amount deducted from the federal tax return because of the two provisions. The belief was that this method placed a taxpayer in the same position for Florida tax purposes as if it had not taken advantage of the two provisions or in the same position as if the two provisions did not exist.

The Issue

Because of the interaction of the federal tax code with the Florida tax code, the adopted method placed a taxpayer choosing to take advantage of the federal provisions in a worse position in Florida than it would have been had it not taken advantage of the federal provisions. In effect, a taxpayer choosing to take advantage of the federal provisions loses the ability to take depreciation deductions in Florida equal to the total amounts taken on the federal return over the life of the asset. A taxpayer taking advantage of the federal provisions would pay higher taxes in Florida than it would if it had not taken advantage of the provisions.

Following is an oversimplified example of the problem using the asset described above -- \$10,000 cost; 5-year useful life; and straight-line depreciation. The first block, labeled **No Bonus** shows the amount of depreciation deductions a taxpayer is entitled to if it does not take advantage of the federal provisions. The second block, **Take Bonus**, shows the effect of the Florida adjustment for those taking advantage of the federal provisions.

	Year 1	Year 2	Year 3	Year 4	Year 5	Total
No Bonus						
Federal	\$2,000	\$2,000	\$2,000	\$2,000	\$2,000	\$10,000
Florida	\$2,000	\$2,000	\$2,000	\$2,000	\$2,000	\$10,000
Take Bonus						
Federal	\$6,000	\$1,000	\$1,000	\$1,000	\$1,000	\$10,000
Florida	\$1,000	\$1,000	\$1,000	\$1,000	\$1,000	\$5,000

The **Take Bonus** block reflects how federal depreciation is applied when a taxpayer elects to take the 50% bonus depreciation – in the first year, the taxpayer receives a \$5,000 deduction, plus \$1,000 regular depreciation deduction (the \$1,000 deduction comes from depreciating the remaining cost of the asset after deducting the amount of the bonus depreciation ($\$10,000 - \$5,000 = \$5,000$) over 5 years. Note that the total federal depreciation totals \$10,000 over 5 years.

For Florida purposes, however, the taxpayer must add the \$5,000 in bonus depreciation taken in the federal return to the Florida return, leaving it with depreciation flowing from the federal return of only \$1,000 per year, for a total of \$5,000.

This result is not what the legislature intended. The Legislature intended to allow a taxpayer taking advantage of the federal provisions to be in the same situation for Florida tax purposes as if it had not

elected to do so. That is, in the example above, the taxpayer would be entitled to \$2,000 per year in depreciation deductions instead of \$1,000.

Legislative and Department of Revenue's Response

The 2008 legislation created a number of problems for Florida corporate taxpayers. Taxpayers had difficult decisions to make regarding whether to take advantage of the bonus depreciation and additional expensing provisions in their federal returns, how to calculate estimated tax payments and how to report these decisions in their financial statements. Also, a number of companies expressed concerns regarding the negative effects of HB 5065 on year-end financial statements and the potential impact on their stock prices.

On November 18, 2008, the President of the Senate and the Speaker of the House sent a letter to the Department of Revenue's Executive Director expressing their intent to have the Legislature consider remedial legislation no later than the 2009 Legislative Session. The letter reiterated that it was not the legislature's intent to place taxpayers in a worse position than they would have been in had they not chosen to take advantage of the federal provisions.

On December 10, 2008, the Department of Revenue adopted Emergency Rule 12CER08-31. The rule relied, in part, on the expressions of legislative intent to not place taxpayer's in a worse situation than they would have been and provided a methodology for taxpayers taking advantage of the federal provisions to adjust their Florida tax returns in order not to be penalized. The rule expires on March 10, 2009.

PROPOSED CHANGES

This bill replaces the statutory changes made last year with a new process to account for bonus depreciation and additional expensing in the Florida tax return. Specifically, the bill spreads out the amount of bonus depreciation or additional expensing claimed by a taxpayer on the federal return over a 5-year period on the Florida return.

The bill accomplishes this by providing that a taxpayer claiming bonus depreciation or additional expensing on its federal return must add 80% of the amount so claimed to Florida taxable income. In each of the 4 subsequent taxable years, the taxpayer can subtract from taxable income 25 percent of the amount by which taxable income was increased. These adjustments to Florida taxable income are available whether the property remains with the taxpayer or is sold or otherwise disposed.

The bill provides that the subtractions may be used by a surviving or acquiring entity following a merger or acquisition. Also, the bill specifically provides that the additions and subtractions can change a taxpayer's net operating loss for Florida tax purposes. Further, the bill requires the Department of Revenue to compromise all penalties and interest imposed on a taxpayer that filed a return prior to the effective date of the bill and subsequently files an amended return based on the provisions of this bill.

The Department of Revenue is granted authority to adopt emergency rules to implement the act.

The bill takes effect upon becoming law and operates retroactively to January 1, 2008.

B. SECTION DIRECTORY:

Section 1. Amends Section 220.03, F.S., to delete changes made last year.

Section 2. Amends Section 220.13, F.S., to delete changes made last year and provide a different method to deal with bonus depreciation and additional expensing.

Section 3. Provides for the compromise of penalties and interest.

Section 4. Grants the Department of Revenue emergency rulemaking authority.

Section 5. Provides an effective date.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

The Revenue Estimating Conference has not met to determine the revenue impact of this bill. However, staff believes the impact is indeterminate. SEE FISCAL COMMENTS BELOW

2. Expenditures:

None

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None

2. Expenditures:

None

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

Florida corporate taxpayers will benefit from being able to fully depreciate assets for Florida tax purposes.

D. FISCAL COMMENTS:

In 2008, the Revenue Estimating Conference (REC) determined that applying the two federal provisions would reduce state revenues in FY 08-09 and 09-10 and increase revenues thereafter. The REC also determined that there was no fiscal impact from HB 5065, adopting the Internal Revenue Code, except for the two provisions. However, the estimate for HB 5065 was done prior to the realization that the language of the bill did not accomplish what the legislature intended. Staff estimates that the fiscal impact of HB 5065 was really positive but indeterminate. The fiscal impact could not be determined because staff does not have sufficient information to determine how taxpayers would have reacted to the loss of the Florida depreciation deductions in determining whether to take advantage of the two federal provisions. Likewise, staff believes that the fiscal impact of this bill is negative, but indeterminate when compared to the effect of HB 5065. The fiscal impact of both bills combined cannot be determined with any accuracy, because it is dependent on the mix of depreciable assets to which the two federal provisions apply. Useful data regarding this mix are not available.

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

Not applicable. This bill does not appear to affect county or municipal government.

2. Other:

None

B. RULE-MAKING AUTHORITY:

The bill grants the Department of Revenue emergency rulemaking authority to implement the provisions of the bill.

C. DRAFTING ISSUES OR OTHER COMMENTS:

None

IV. AMENDMENTS/COUNCIL OR COMMITTEE SUBSTITUTE CHANGES