



# TPPF Annual Policy Orientation

**Rep. Dan Branch**

**Member, Texas House of Representatives**

*Downtown, Uptown, Near North & East Dallas, Park Cities – District 108*

**Select Committee on Higher & Public Education Finance**

*Chairman*

**Public Education Committee**

*Chairman of Budget and Oversight*

**Appropriations Committee**

*Vice Chair, Education Subcommittee*

**Calendars Committee**

**January 10, 2008**

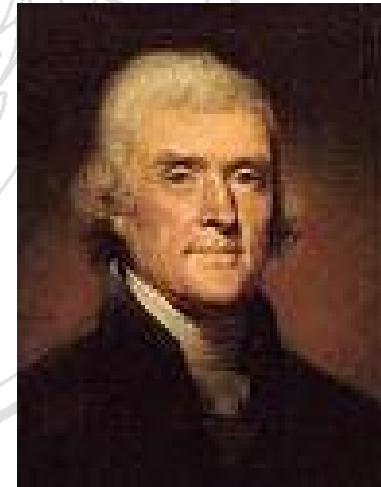
**Austin, Texas**



# Limited Govt. Tradition

***"My reading of history convinces me that most bad government results from too much government."***

**-- Thomas Jefferson**





# Revised Franchise Tax

- I. Revised Franchise Tax Overview**
- II. Economic Outlook for Texas:  
Taxation & Spending**
- III. Future Implications: Challenges  
of 21st Century Limited  
Government**



# Road to Revised Franchise Tax

- ★ **78th Special 2004: Franchise tax reform debate**
- ★ **79th Session + 2 Specials: Continued franchise tax debate**
- ★ **Nov 2005: *West Orange Cove* ruling; Gov. Perry's Texas Tax Reform Commission commences statewide stakeholder meetings**
- ★ **March 2006: Commission report released**
- ★ **May 2006: HB 3 Passed Legislature & signed by Governor**



# Road to Revised Franchise Tax

- ★ Jan - May 2007: Franchise Tax Clean-up Bill Debated & Passed (**HB 3928**)
- ★ Late 2007 - Present: Comptroller rulemaking
- ★ May 2008: 1st Revised Franchise tax collections



# 2006 School Finance Solution

- ★ HB 1: **33.3%** cut in M&O property tax rate, revenue cap & education/equity reforms
- ★ HB 2: Dedicates new franchise tax revenue to property tax reduction
- ★ HB 3: Revised franchise tax
- ★ HB 4: Revised used car tax
- ★ HB 5: Tobacco tax increase



# Property Tax Cut Savings

(Sample Residence)

- ★ Home Value = \$265,000
- ★ M&O Before = \$3,750  
(inc. homestead exemption @ \$1.50 cap)
- ★ M&O After = \$2,500  
(\$1.00 per \$100 of value)

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- ★ Total Savings = \*\$1,250



\* Tax payment due 1/31/08



# Property Tax Cut Savings

(Sample Business)

★ **Property Value \$2,750,000**

★ **M&O Before \$41,250**  
(@ \$1.50 cap)

★ **M&O After \$27,500**  
(\$1.00 per \$100 of value)

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★ **Total Savings = \*\$13,750**

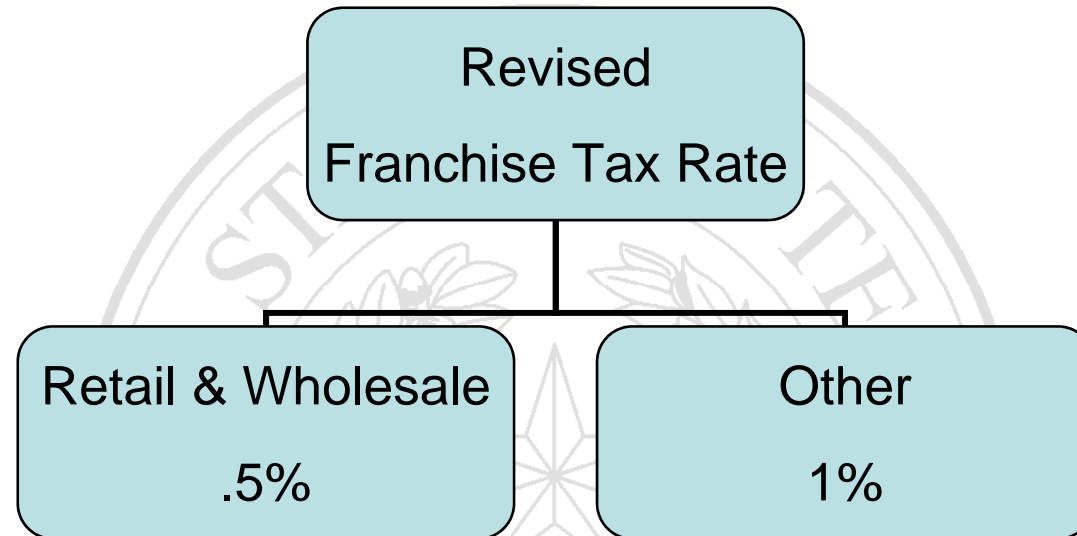


\* Tax payment due 1/31/08



# Revised Franchise Tax

## *Basic Structure*



***Business margin = gross receipts less  
Deduct direct labor or costs of goods sold***

★ **Choice #1** - Deduct labor, compensation, benefits **OR**

★ **Choice #2** - Deduct costs of goods sold

***Multiply applicable rate times the difference***



# Revised Franchise Tax

## Old Franchise Tax

- ★ Applied to Corporations & LLCs
- ★ Rate - greater of **4.5%** of net income or **.25%** of capital
- ★ \$150,000 small business exemption

## Revised Franchise Tax

- ★ Applies to Corporations, LLCs and LPs
- ★ Rate - ranges from **0.7%** of receipts to **0.5% or less** after
- ★ \$300,000 small business exemption

**\*\* Sole Proprietors, General Partnerships w/ natural persons, certain passive entities & non-profits exempted under old & revised franchise tax**



# Small Business Protections

- ★ **Businesses grossing up to \$300,000 owe no tax**
- ★ **Businesses w/ tax liability up to \$1,000 owe no tax**
- ★ **Graduated small business discount for entities with up to \$900,000 in revenue\***
- ★ **E-Z computation for businesses with revenue up to \$10 million (.575%)**

*\* see chart*



# Small Business Protections

## Small Business Discount Rates

<b>Taxable Entity with Annual Total Revenue</b>	<b>Discount on Tax Liability</b>
<b>At least \$300,000 but less than \$400,000</b>	<b>80%</b>
<b>At least \$400,000 but less than \$500,000</b>	<b>60%</b>
<b>At least \$500,000 but less than \$700,000</b>	<b>40%</b>
<b>At least \$700,000 but less than \$900,000</b>	<b>20%</b>



# 2008 Revised Franchise Tax Projections

## ★ Estimated revised franchise tax filers

- ★ **2,805,000** business entities in TX
- ★ **1,985,000 (71%)** sole proprietors – do not file
- ★ **750,000 (27%)** to file returns - 680,000 in 2006
- ★ **200,000 (7%)** to owe tax at some level – 160,000 in 2006

## ★ Savings for small businesses

- ★ **\$300m** - small business discounts/exemptions
  - ⇒ 485,000 businesses under \$300K in total revenue
  - ⇒ 97,000 business between \$300K – \$900K in total revenue
- ★ **\$18 million** – EZ Calculation (10K – 15K businesses)

Source- Comptroller of Public Accounts

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# School Finance Solution

- ★ '08-'09 estimated new revenue from School Finance Solution Package – **\$8.2 B\***
  - ★ \$6.15b\* in new franchise tax revenue
  - ★ \$1.44b\* in new tobacco tax revenue
  - ★ \$25.2m\* in new vehicle sales tax revenue
  - ★ \$20.1m\* in new interest / other
- ★ '08-'09 **local property tax relief - \$14.2 B**
- ★ **Net Tax Cut = \$6 Billion**

Source- Comptroller of Public Accounts

\*Biennial calculations

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# Economic Outlook

## Texas Budget Growth

<b><i>Excluding</i> \$14.2 B in Property Tax Relief</b>	<b>2002-03 Budget (in millions)</b>	<b>2008-09 Budget (in millions)</b>	<b>Average Yearly Growth</b>
<b>General Revenue</b>	\$60,212.9	\$74,071.4	<b>3.3%</b>
<b>All Funds Total</b>	\$115,678.7	\$153,774.2	4.7%

<b><i>Including</i> \$14.2 B in Property Tax Relief</b>	<b>2002-03 Budget (in millions)</b>	<b>2008-09 Budget (in millions)</b>	<b>Average Yearly Growth</b>
<b>General Revenue</b>	\$60,212.9	\$80,184.5	<b>4.7%</b>
<b>All Funds Total</b>	\$115,678.7	\$167,965.3	6.5%

**\*\* TX avg. yearly Inflation + Population Growth Rate 2000 – 2007 = 4.7%**



# TX Budget & Economic Indicator Comparison

## REVENUE CATEGORY

## ECONOMIC INDICATOR

*Avg. Yearly GR Growth	3.3%
*Avg. Yearly All Funds Growth	4.7%

**VS.**

**Avg. Yearly Population + Inflation Growth	4.7%
**Avg. Yearly Personal Income Growth	6.1%
**Avg. Yearly Gross State Product Growth	7.0%

*\* '02-'09 Revenue Excluding Property Tax Relief*

*\*\* Economic Indicator Rates – Yearly Average 2000 - 2007*



# Economic Outlook

## *Large States*

State	Rank Per Capita Tax Burden	Rank of Return on F. Tax Dollar
<b>Texas</b>	<b>5th</b> <b>\$6,432</b>	<b>1st</b> <b>\$0.97</b>
<b>Florida</b>	<b>4th</b> <b>\$7,620</b>	<b>2nd</b> <b>\$0.95</b>
<b>Illinois</b>	<b>3rd</b> <b>\$7,844</b>	<b>5th</b> <b>\$0.78</b>
<b>California</b>	<b>2nd</b> <b>\$8,047</b>	<b>4th</b> <b>\$0.80</b>
<b>New York</b>	<b>1st</b> <b>\$8,758</b>	<b>3rd</b> <b>\$0.82</b>

**SOURCES:** *Northeast-Midwest Institute staff calculations based on 2005 U.S. Department of Commerce, Bureau of the Census, annual Consolidated Federal Funds Report, and The Tax Foundation, annual Special Report: Federal Tax Burdens and Expenditures by State.*



# Economic Outlook

## *Texas Leads Large States*

- ★ **2007 ALEC Study assessing economic competitiveness findings based on 16 policy variables (taxes, regulation, etc...)**

Large State Rank	State	50 State Rank
1st	Texas	10th
2nd	Florida	14th
3rd	California	41st
4th	New York	42nd
5th	Illinois	49th

*Source- American Legislative Exchange Council Report: "Rich States Poor States"*



# Economic Outlook

## Summary

- ★ **Texas – low taxes, limited regulations**
  - ★ **Per capita state tax burden – 49th ranking  
(2nd lowest in US)**
  - ★ **Per capita spending – 42nd ranking  
(8th lowest in US)**
- ★ **Texas - Surging growth, economy**
  - ★ **Fastest growing state in raw numbers  
(6th in % growth)**
  - ★ **Approx. 490,000 New Texans per year / 1,350 per day**
  - ★ **10th – 11th largest world economy  
(GSP- \$1.06 trillion)**
  - ★ **#1 Exporter in US (4 years)**



# Texas Matters...

★ **National & International implications if we fail to manage growth & not address current/future infrastructure needs**

- ★ **Energy/Air Quality**
- ★ **Water**
- ★ **Mobility**
- ★ **Public/Social Safety Nets**
- ★ ***Educated Workforce***



# Texas Matters...

## *21st Century Challenges:*

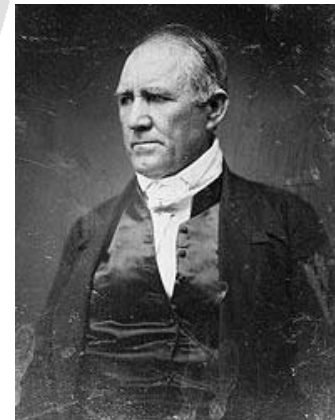
- ★ **Preserving our limited government tradition**
  - ★ **limited (not anorexic) spending, limited debt**
  
- ★ **Managing our growth & success**
  - ★ **infrastructure challenges – not under investing, long lead times**



# Texas Matters...

- ★ ***“The benefits of education... generally diffused through a community, are essential to the preservation of a free government.”***
- ★ ***“Texas will... lift it’s head and stand among the nations... for no country upon the globe can compare with it in natural advantages.”***

**-- Sam Houston**





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