

2021

Revenue Estimating and Tax Research Conference

Federation of Tax Administrators

The Texas Franchise Tax

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Margin Tax Formula

Total revenue (from applicable IRS form)

- Greatest of:

Cost of Goods Sold (COGS)

Compensation

30% of Total Revenue

\$1 million

= Margin before apportionment

X Apportionment factor

= Apportionment margin

- Allowable deductions

= Taxable margin

X Tax rate (0.375% or 0.75%)

= Tax due on margin before credits

- Credits

= Net tax due

EZ Computation Formula

Total Revenue (from applicable IRS form)

X Apportionment factor

= Taxable margin

X Tax rate (0.331%)

= Net tax due



2019 Franchise Tax Report Information

Deduction Type	Reported Tax (\$Thousands)	Share %				
Cost of Goods Sold	2,378,750	56.6%				
Compensation	504,329	12.0%				
30% of Total Revenue	701,857	16.7%				
\$ 1 Million	54,636	1.3%				
EZ Computation	563,167	13.4%				
Total	4,202,739	100.0%				

- Annual Franchise Tax Reports are due May 15, representing prior year's activity.

2020 and 2021	
Item	Amount
No Tax Due Threshold	\$1,180,000
Tax Rate (retail or wholesale)	0.375%
Tax Rate (other than retail or wholesale)	0.75%
Compensation Deduction Limit	\$390,000
EZ Computation Total Revenue Threshold	\$20 million
EZ Computation Rate	0.331%

- Each taxable entity must file a Franchise Tax Report:
 - No Tax Due;
 - EZ Computation; or Long Form; and
- Information Report:
 - Public Information Report; or
 - Ownership Information Report

Franchise Tax History

- **ENACTED**

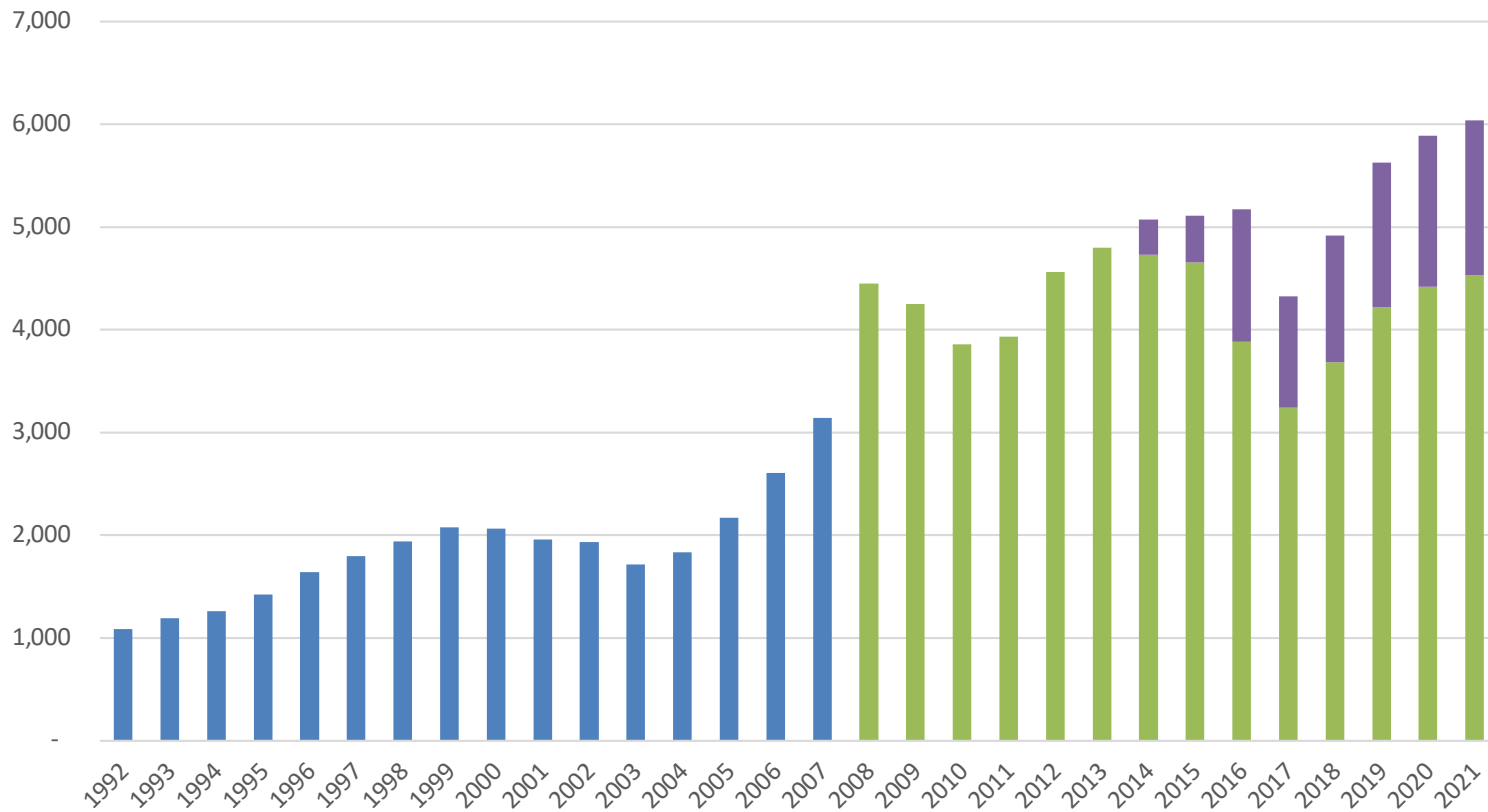
- 30th Legislature (1907) \$0.50 per \$1,000 of taxable capital

- **RATE AND BASE CHANGES**

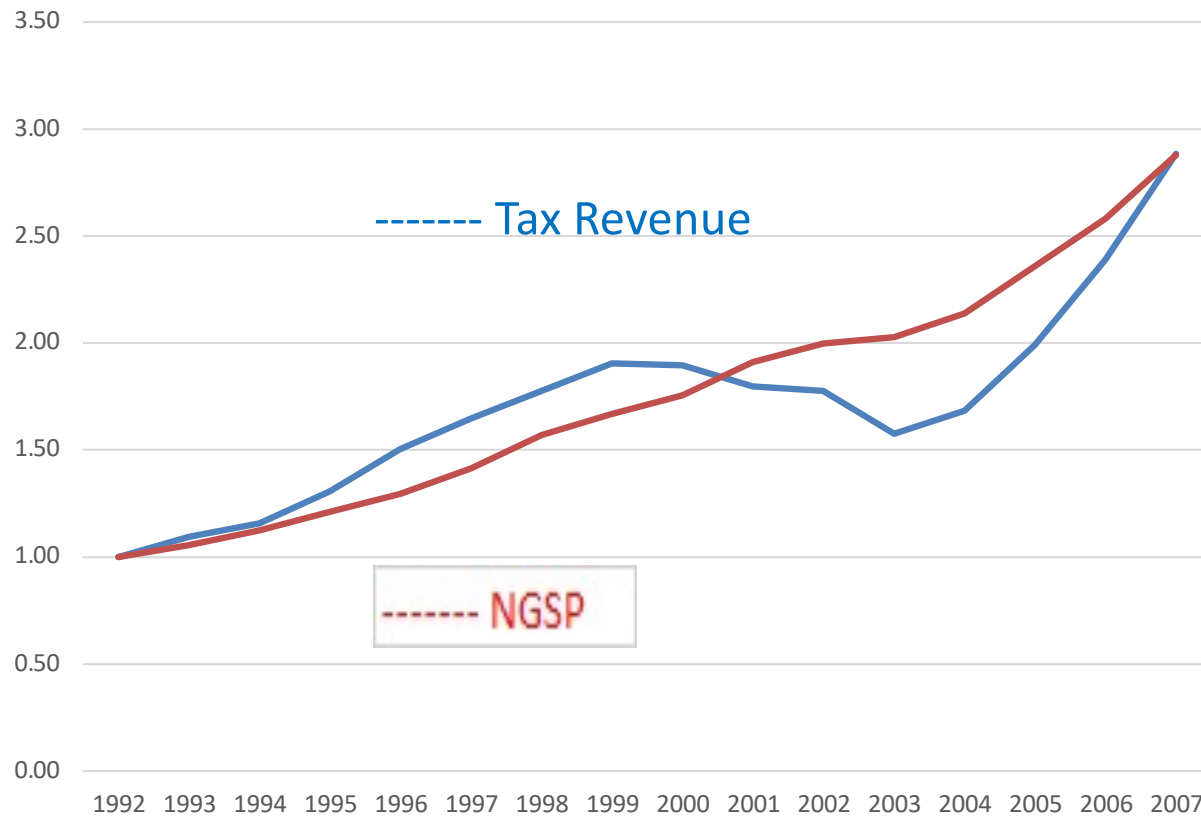
- There were seven rate increases and two rate reduction between 1938 and 1971
- 62nd Legislature (1971) Raised surtax to \$1.75 (effective rate \$4.50); surtax dropped by \$0.25 to \$1.50 (effective rate \$4.25) from 1972 to 1974
- 64th Legislature (1975) \$4.25 basic rate — \$55 minimum tax; debt became exempt; no surtax
- 68th Legislature (1984) \$5.25 basic rate — \$68 minimum tax; banks became taxable (eff.5/1/85)
- 70th Legislature (1987) \$5.25 basic rate plus \$1.45 surtax — \$150 minimum tax effective for 1988 and 1989 reports; rate reverted to \$5.25 with no surtax — \$68 minimum tax for reports due in 1990
- 72nd Legislature (1991) \$2.50 per \$1,000 of taxable capital and amount, if any, by which a tax of 4.5% on earned surplus exceeds the tax on capital
- 79th Legislature, 3rd Called Session (2006) One percent of a firm's Texas-apportioned "margin," defined as total revenue less the greater of the cost of goods sold, total compensation, or 30% of total revenue; a half-rate of 0.5% applies to businesses in retail and wholesale trade (eff.01/01/08)
- 82nd Legislature, 1st Called Session (2013) Tax Refund for Economic Development, Reinvestment Zone/Abatement Agreement (Revenue Object 3804) was repealed
- 83rd Legislature (2013) Temporary tax rates of 0.975% in 2014 and 0.95% in 2015 for most taxpayers; 0.4875% in 2014 and 0.475% in 2015 for businesses in retail or wholesale trades; a fourth margin calculation of Total Revenue minus \$1 million is available (eff.1/1/14)
- 84th Legislature (2015) Tax rates permanently reduced to 0.75% for most taxpayers and 0.375% for businesses in retail or wholesale trades (eff.1/1/16)



Franchise Tax Revenue
(\$ Millions)
Earned Surplus 1992 - 2007
Margin 2008 - 2021

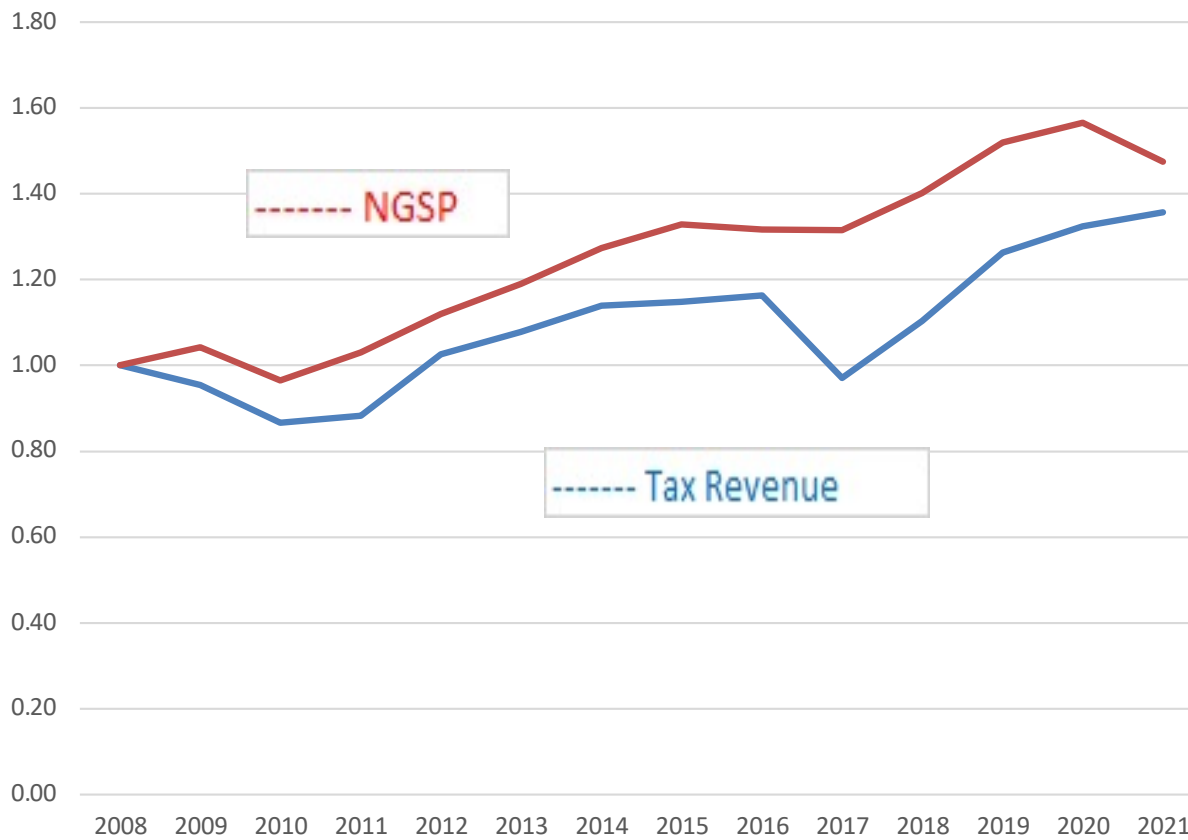


Franchise (Earned Surplus) Tax Revenue vs. Nominal Gross State Product



Adjusted R Square	0.81
Coefficient of Variation	0.27

Franchise (Margin) Tax Revenue vs. Nominal Gross State Product



Adjusted R Square	0.78
Coefficient of Variation	0.14

2007 vs 2019 Franchise Tax Reports

<u>Industry</u>	<u>2007 Tax</u> <u>(\$Thousands)</u>	<u>2007</u> <u>Share</u>	<u>2019 Tax</u> <u>(\$Thousands)</u>	<u>2019</u> <u>Share</u>
Agriculture	14,638	0.49%	13,416	0.32%
Mining	478,068	16.11%	232,794	5.54%
Utilities & Transportation	180,037	6.07%	200,687	4.78%
Construction	112,422	3.79%	260,683	6.20%
Manufacturing	540,389	18.21%	522,268	12.43%
Trade	558,075	18.81%	630,927	15.01%
Information	97,120	3.27%	246,809	5.87%
Fin Ins RE	342,582	11.54%	584,576	13.91%
Other SVS	607,732	20.48%	1,396,422	33.23%
Not Coded	36,601	1.23%	114,157	2.72%
Total	2,967,665	100.00%	4,202,739	1.00

Margin Tax Estimates vs. Actual

(\$Thousands)

	Estimated	Actual	Difference
2008	5,884,262	4,451,326	1,432,936
2009	6,045,568	4,250,332	1,795,236
2010	6,396,469	3,856,866	2,539,603
2011	6,967,725	3,932,114	3,035,611

Franchise Tax Margin Base First Year Results – Detailed Analysis

Expected	Expected		Unexpected	Unexpected	
	<u>Estimated</u>	<u>Actual</u>		<u>Estimated</u>	<u>Actual</u>
Apportionment Ratio	6.52%	6.62%	Percentage of Texas Revenue Using COGS (\$1,844 Billion Estimate) (\$2,098 Billion Actual)	79.70%	84.70%
Texas Revenue (Billions)	\$1,844	\$2,098			
Overall Tax Rate	0.89%	0.89%	Deduction Share for For COGS Deductors	68.40%	81.90%
Credits/Discounts (Millions)	\$380	\$370			

Policy Issues

- Cost of Goods Sold (COGS)
- Taxation of Partnerships and Other Pass-through Entities
- Apportionment of Services
- Reduced tax rate for retailers/wholesalers
- Two-Tier Tax System
- R&D Credit

Research and Development Activities Credit

	New R&D Credit Claimed	New R&D Credit Carryforward	Old R&D Credit Claimed	Old R&D Credit Carryforward
2019	\$251,929,225	\$900,593,645	\$7,031,571	\$243,600,243
2020	\$274,484,603	\$1,073,396,423	\$3,827,495	\$236,899,079