MEMORANDUM

OKLAHOMA TAX COMMISSION
TAX POLICY AND RESEARCH

DATE: April 2, 2012

SUBJECT: HB 3038 Committee Substitute (Req. No. 3342)

TO: Rick Miller, Director

FROM: Michael C. Kaufmann, Tax Policy Analyst

The Proposed Committee Substitute for Engrossed HB 3038 amends the apportionment of sales tax collections; proposes an individual income tax rate reduction beginning with tax year 2013 with a trigger mechanism to allow for further rate reductions; eliminates all income tax credits and almost all deductions, exemptions, and exclusions for individual income tax filers beginning with tax year 2013.

Section 1 – Apportionment of Sales Tax Collections
Section 1 amends 68 O.S. § 1353 which relates to the apportionment of sales tax collections. This measure modifies the apportionment of sales tax increasing the allocation to the Teachers' Retirement System Dedicated Revenue Revolving Fund by 1.5%; adding an allocation of .5% to the Ad Valorem Reimbursement Fund and decreasing the amount apportioned to the General Revenue Fund ("GRF") by 2% effective for FY 14. Additionally, for FY 19 and thereafter, this Section apportions an additional .25% for a total of .75% to the Ad Valorem Reimbursement Fund and decreases the amount apportioned to the GRF by .25%.

Section 2 – Income Tax
Amends 68 O.S. § 2355(B), which is the individual income tax rate structure, by enacting an individual income tax rate reduction beginning with tax year 2013 (2.5%) with a trigger mechanism in Section 3 to allow for further rate reductions.

Further, no tax is imposed on single filers with Oklahoma taxable income equal to or less than Eight Thousand Seven Hundred Dollars ($8,700.00) and for married filers with Oklahoma taxable income equal to or less than Fifteen Thousand Dollars ($15,000.00).

Section 3 – Trigger
Section 3 proposes to enact a "trigger" mechanism whereby further income tax rate reductions may be authorized. The State Board of Equalization, at their February 2014 meeting, is to set an initial

baseline amount consisting of revenue collections for FY 13 from motor vehicle collections under 47 O.S. § 1104, sales and use tax collections under 68 O.S. § 1354 and § 1402, and corporate income tax under 68 O.S. § 2355 (D). The revenue estimates for FY14 for like revenue collections are then compared to the initial baseline, which might result in revenue growth. If revenue growth is at least 5% greater than the initial baseline, then the individual income tax rate is reduced by 0.25% for the tax year beginning the next January 1. For the February 2014 meeting, if the revenue growth is 5%, then tax year 2015 individual income tax rate would be reduced to 2.25%. If the finding in the February 2014 meeting does allow for the income tax rate to be reduced, then the next time the State Board of Equalization is authorized to reduce the rate is February 2016 for tax year 2017.

Section 4 - Income Tax
Adds a new section of law, 68 O.S. § 2355.3, eliminating all income tax credits, and almost all deductions, exemptions and exclusions for individual income tax filers beginning with tax year 2013. The following exemptions would still be allowed: retirement benefits from public pension systems, Social Security benefits, retirement benefits from non-public pension systems, military retirement benefits, and civil service retirement benefits in lieu of Social Security. The deduction for active duty military compensation as well as the exclusion for certain deferred compensation distributions would also still be allowed[1].

Fiscal Impact:

Sales Tax
Based on the February 2012 FY 13 revenue forecast, a $45,710,000 decrease in sales tax collections designated for GRF will occur for FY 14, with $34,282,000 apportioned to the Teachers' Retirement System Dedicated Revenue Revolving Fund and $11,427,000 apportioned to the Ad Valorem Reimbursement Fund for FY 14.

Based on the February 2012 FY 13 revenue forecast, a $5,714,000 decrease in sales tax collections designated for GRF will occur for FY 19, with $5,714,000 apportioned to the Ad Valorem Reimbursement Fund.

Income Tax (Sections 2 and 4)
The data for the current model is from tax year 2009 individual income tax returns and simulating certain growth assumptions for tax years 2013 and 2014. Individual income tax revenue is estimated for tax years 2013 and 2014 under current law; and then estimated for each tax year under the proposed law changes. The difference is then calculated, resulting in the estimated impact by tax year.

The Oklahoma Individual Income Tax Micro-Simulation Model was used to develop the impact of this proposal for tax years 2013 and 2014. For tax year 2013, the expected fiscal impact is a decrease of $580,982,000 and for tax year 2014 the decrease is expected to be $659,406,000. Table 1 below

[1] Also allowed as either exemptions or deductions are interest from U.S. Government obligations, Railroad Retirement benefits, out of state income, and certain exempt tribal income. Either as a result of federal law or court cases, these items cannot be taxed by Oklahoma.

shows the fiscal year impact of the income tax portion of this proposal.

Table 1			
Fiscal Impact			
Tax year 2013	-$580,982,000		
Tax year 2014	-$659,406,000		
FY CONVERSION (assuming 40%/60%)		FY13	FY14
Tax year 2013	-$580,982,000	-$232,393,000	-$348,589,000
Tax year 2014	-$659,406,000		-$263,762,000
	FY TOTAL	-$232,393,000	-$612,351,000
Source: Oklahoma Individual Income Tax Micro-simulation model			