Multistate Tax Update: December 3, 2015

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States extend historic preservation tax credits

NORTH CAROLINA

An article in *The News & Observer* this past summer opined on the state of historic tax credits in the Tar Heel State. The article cited a legislator who lamented the fact that in the economic development arena, "South Carolina is eating our lunch," and the president ofPreservation North Carolina, Myrick Howard, agreed that North Carolina is losing its advantage in the preservation of architectural and historic resources.

Myrick attributed this to the December 2014 sunset of tax credits that made it easier to rehabilitate historic structures. Indeed, he declared, the effects of the tax credit were tangible: The private sector spent nearly $2 billion to revive key areas throughout the state, like downtown Durham, Raleigh, Winston-Salem, Asheville, Salisbury, Mount Airy, New Bern, and Edenton during the existence of the tax credit.

However, tax credits are not without controversy. Some opponents claim that these kinds of tax credits go against tax reform and leave local governments without skin in the game. Nevertheless, support for the tax credits is generally widespread, and Howard observed, "[p]robably no tax incentive in North Carolina has generated a better return for the state in jobs, economic development, and community livability and pride. Without this incentive, North Carolina is losing out; jobs and investors are leaving the state in droves. Buildings are sitting empty."

Recognition of the economic impact of the credits is evident in the 2015-17 budget. Lawmakers renewed the tax credits on income producing properties, effective Jan. 1, 2016. They also allocated $8 million of general funds for the biennium.

The budget specifies that a taxpayer who is allowed a federal income tax credit for making qualified rehabilitation expenditures for a certified historic structure is allowed a state tax credit as follows:

- 15 percent for expenses up to $10 million
- 10 percent for expenses between $10 million and $20 million

The budget also establishes the following bonus credits:

- A development tier bonus of 5 percent of qualified rehabilitation expenditures, up to $20 million if the certified historic structure is located in a development tier one or two area.
- A targeted investment bonus of 5 percent of qualified rehabilitation expenditures, up to $20 million, if the certified historic structure is located on an eligible targeted investment site.

The maximum amount of credit allowed is $4.5 million. Additionally, the tax credit may not exceed the amount of tax owed by the taxpayer, and any unused portion of the credit may be carried forward for 9 years.

These credits are scheduled to sunset on Jan. 1, 2020.

GEORGIA

Similarly, the Peach State revised its tax credit for the rehabilitation of historic structures by way of House Bill 308.

Effective Jan. 1, 2016, Georgia will allow a tax credit for the rehabilitation of certain certified historic structures, up to $5 million. If the project creates 200 or more full-time permanent jobs, or $5 million in annual payroll within two years of the placed in service date, the project is eligible for credits of up to $10 million. It should be noted that the credit for certified historic homes is capped at $100,000 in any 120-month period.

All or a portion of any historic preservation tax credits claimed, but unused, may be transferred or sold to another Georgia taxpayer under certain conditions.

“Many states are improving their Historic Tax Credits to revitalize historic areas. A big change to look out for is the transferability of state credits, which can help developers partially finance a project,” mentioned a PRNewswire article.

Michigan: Governor signs the state’s largest investment in transportation funding in 50 years

Gov. Rick Snyder has signed a package of bills “implementing the state’s legislative solution to infrastructure funding.” This leaves “Michiganders [with] safer roads and stronger bridges to travel on...Now we have a commonsense plan of action to improve our roads and make government more efficient and accountable,” touted a Nov. 10, 2015, governor’s office press release.

Key components of the package include the following:

- HB 4738: Enacting a 7.3 cents increase on the current 19 cent fuel tax, bringing it up to 26.3 cents per gallon for all motor fuels, including diesel and natural gas, starting Jan. 1, 2017. Beginning Jan. 1, 2022, the tax rate will be indexed to inflation, to ensure ongoing viability of the increase.
- HB 4614: Applying the truck fuel tax to natural gas, and gas used by interstate trucks, starting Jan. 1, 2017.
- HB 4616: Tying the tax rate on diesel fuel to the same level as the tax on gasoline, making the per-gallon rate equal for all fuels.
- HB 4736: Increasing registration and truck weight fees by 20 percent. It also creates an annual plug-in hybrid vehicle surcharge of $30, and an annual electric vehicle surcharge of $100.
- HB 4737: Restricting the administrative expenses of Michigan’s State Trunkline Fund at the Michigan Department of Transportation to 8 percent of expenditures, down from 10 percent. HB 4737 also requires warranties on all local road projects over $2 million.

The State Trunkline Fund is a bond financing program for transportation projects. This law also creates a task force to study materials and methods for longer lasting roads.

In order to offset the impact of these increases on taxpayers, lawmakers enacted two additional bills:

- HB 4370: Effective with the 2018 tax year, increases the homestead property tax credit from $1,200 to $1,500 and expands the eligibility for the credit from households earning $51,000 or less to those earning $61,000 per year or less. It also extends part of that credit to renters, at the rate of 23 percent of rent paid, up from 20 percent.
- Senate Bill 414: Rolling back the individual income tax rate in any year that the state General Fund revenue exceeds 1.425 times the rate of inflation, beginning in 2023.

The last time Michigan implemented an infrastructure plan was in 1997. Gov. Snyder noted that this one raises 20 percent more revenue, and includes a mechanism for adjusting for inflation to ensure sustainability and maintain buying power. Approximately 61 percent of the revenue will go to local road agencies in communities across the state, and the remaining 39 percent will be dedicated to state highways. Detroit will be permitted to use up to 20 percent of its funding for mass transit, and all other localities may use up to 10 percent for the same purpose.

MLive noted that the gas tax and vehicle registration increases would generate $600 million in annual revenue, and that starting in 2019, the state will allocate another $600 million in general fund revenue.

Despite the much needed infrastructure solution, House Minority Leader Tim Greimel (D-Auburn Hills) characterized the infrastructure plan as “a sham. It's a joke. It's pretense…not a real fiscally responsible solution." Likewise, Senate Minority Leader Jim Ananich (D-Flint) complained that “[t]his plan won't fix our roads. It will, however, create new problems that will need to be fixed later.”

On the other hand, MLive quoted Senate Majority Leader Arlan Meekhof (R-West Olive) who conceded that while the task of funding infrastructure was not easy, "[f]rom the very beginning, it was very clear that fixing Michigan's roads would be a key to fixing Michigan…I'm proud of all my colleagues."

Michigan was not likely to be able to address the “sorry state of its roads” any other way. In May, voters rejected a ballot measure that would have increased the gas tax to 41.7 cents. At that time, the House Fiscal Agency estimated that the tax increase would have generated more than $1.6 billion per year, with $1.2 billion going towards roads, $130 million to mass transit, $300 million to the school aid fund, and $95 million to local governments.

Tax Foundation issues its 2016 State Business Tax Climate Index

The Tax Foundation describes itself as “the nation’s leading independent tax policy research organization.” As a Washington, D.C.-based non-partisan, non-profit research think tank, the group publishes a variety of reports on many state and federal tax topics. The most recent is its popular 2016 State Business Tax Climate Index (Index), which is designed to show how well states structure their tax systems and provide a roadmap for improvement. The Index does not purport to measure economic opportunity or freedom, or even the broad business climate, but rather the narrower business tax climate.

This year, the top 10 states are:

1. Wyoming
2. South Dakota
3. Alaska
4. Florida
5. Nevada
6. Montana
7. New Hampshire
8. Indiana
9. Utah
10. Texas

The bottom 10 are:

41. Maryland
42. Ohio
43. Wisconsin
44. Connecticut
45. Rhode Island
46. Vermont
47. Minnesota
48. California
49. New York
50. New Jersey

In evaluating each state’s tax climate, researchers considered more than 100 variables. Among these is the presence or absence of a major tax, like an income tax, the complexity of a state’s tax code, and the extent to which the state imposes non-neutral taxes with relatively high rates.

Researchers analyzed variables within five categories, which were then weighted by the variability of the 50 states’ scores from the mean: individual income tax, sales tax, corporate tax, property tax, and unemployment insurance tax.

The following are some interesting observations from the analysis:

> **INDIVIDUAL INCOME TAX: ONE-THIRD OF THE TOTAL SCORE**
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> This category compares states which tax individual income. The five states which do not impose an individual income tax and received a perfect score, include Alaska, Florida, Nevada, South Dakota, and Wyoming. These states also ranked very high overall, at numbers 3, 4, 5, 2, and 1, respectively.
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> Although Texas and Washington do not have an individual income tax, they do not have perfect scores in this component because they tax limited liability and S-corporation income through their gross receipts taxes.

California has the highest top income tax rate, 13.3 percent, and an overall ranking of 48. North Dakota, ranked number 26 overall, has the lowest individual income tax rate, 2.9 percent.

SALES TAX: 22 PERCENT OF THE TOTAL SCORE

Sales taxes levied on the purchase of goods at the point of sale, and including excise taxes on specific items like liquor, tobacco, and gas, vary in amount and structure. Researchers looked at actual rates, which, if too high, could cause business to be lost to lower-tax locations, resulting in lost profits, jobs, and tax revenue. The Index ranked Delaware first in this category, and Louisiana at number 50.

Colorado, whose 2.9 percent rate is the lowest, ranked 18 overall on the Index. California has the highest sales tax, 7.5 percent, and it ranks 48 overall.

CORPORATE TAX: 18.5 PERCENT OF THE TOTAL SCORE

This category was designed to gauge how a state's corporate income tax top marginal rate, bracket structure, and gross receipts rate affect its competitiveness compared to other states, as the extent of taxation can affect a business's level of economic activity within a state.

Part of the reason Wyoming and South Dakota achieved the top two spots overall is that neither state levies a corporate income tax or a gross receipts tax.

In contrast, Iowa's 12 percent corporate income tax rate qualifies for the worst ranking among states that levy a corporate income tax, followed by Pennsylvania's 9.99 percent rate. These states are ranked at numbers 40 and 32 overall, respectively.

PROPERTY TAX: 14.8 PERCENT OF THE TOTAL SCORE

This component includes taxes on both real and personal property. The Index notes that property taxes are a significant factor in business location decisions, and that a 10 percent increase in business property taxes decreases the number of new plants opening in a state by between 1 and 2 percent. Local property taxes are perceived as an unfair state or local tax in part because when property values fall through no fault of the owners, as they did in the recent economic downturn, localities respond by increasing the tax rates to make up for lost revenues.

New Mexico and Utah had the two most favorable property tax ranks, and overall, they ranked at numbers 35 and 9, respectively. The states with the least favorable ranks were Iowa and Connecticut. Overall, they ranked at numbers 40 and 44, respectively.

UNEMPLOYMENT INSURANCE TAX: 11.13 PERCENT

Every state levies an unemployment insurance (UI) tax. They are complex, variable-rate systems that impose different rates on different industries and different bases, depending upon such factors as the health of the state's UI trust fund.

The “shut down” effect of the UI tax is one of its worst features because financially troubled firms, for which survival may involve laying off employees, actually pay higher marginal rates as they are forced into higher tax rate schedules.

States that had favorable UI rankings have rate structures with lower minimum and maximum rates and a wage base at the federal level, and have not complicated their systems with benefit add-ons and surtaxes, among other things.

States with the least damaging UI taxes are Oklahoma, Nebraska, Florida, Delaware, and Louisiana. These states rank 33, 27, 4, 14, and 37 overall, respectively.

States with the most damaging UI taxes are Pennsylvania, Rhode Island, Michigan, Massachusetts, and Kentucky. These states rank 32, 45, 13, 25, and 28 overall, respectively.

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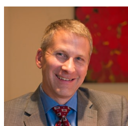
STATES ON THE MOVE

Several states had notable overall ranking changes this year. For example, Illinois improved significantly, from 31 to 23 overall. This progression was due to the sunset of corporate and individual income tax increases that were first imposed in 2011 to address the state's backlog of unpaid bills.

In North Carolina, the 2013 reforms had a substantial impact on the ranking; the state jumped from number 44 last year to number 15 this year. Significant changes included cutting the corporate income tax, from 6.9 percent to 6 percent last year, which fell again to 5 percent in 2015. Additionally, the individual income tax, which lawmakers converted to a single-rate tax of 5.8 percent from a graduated rate tax with a top marginal rate of 7.75 percent in 2014, saw a further modest cut in 2015, decreasing to 5.75 percent. Further reductions are scheduled through 2017.

Next, although New York retains its rank of number 49 overall for this year, the corporate reform tax package that lawmakers enacted will likely create an improvement in next year's position. The enacted changes include reducing the corporate income tax rate from 7.1 percent to 6.5 percent, and eliminating the capital stock tax, among other things.

Finally, Kansas, which has been in the news frequently this year for its dismal economy caused by overzealous tax cuts, fell three rungs due to its sales tax increase from 6.15 to 6.5.



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