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Tax Credit Review Commission Offers Recommendations to Curb Growth in Tax Credits

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Since 1998, Missouri's redeemed tax credits have grown by 408 percent, while General Revenue has grown by only 14 percent.* Given this growth, Governor Nixon appointed the Tax Credit Review Commission in July with the task of reviewing the state's tax credits and making recommendations "for greater efficacy and enhanced return on investment." The Commission discussed several global issues and took a detailed look at each of the individual 61 tax credits, which were worth more than $500 million in both 2009 and 2010. While the recommendations are not binding, they could be the starting point for discussion during the 2011 session. If all of the recommendations were enacted, a savings of $220 million could be achieved.

Recommendations Regarding Global Issues

The Commission made several recommendations about global issues that impact most or all tax credits. The Commission recommends that the state:

- Maintain the existing policy that excludes tax credits from the annual appropriations process.
- Revise schedules for sunsetting (ending) tax credits: Banking and Insurance Tax Credits should have a two year sunset; Distressed Communities, Economic Development, Agriculture and Environment Tax Credits should have a four year sunset; Historic Preservation, Low Income Housing and the Social/Contribution Tax Credits (e.g. Neighborhood Assistance Program, Food Pantry, etc.) should have a six year sunset.
- Impose limitations on tax credits authorized annually (some tax credits already have limits).
- Establish ways for the state to buy back outstanding tax credits at a discount. For instance, the state could allow a Low Income Housing Tax Credit certificate to be offered in lieu of an allocation already approved for a project. The transferred tax credit would be at a lower dollar amount than originally authorized, which would allow the state to "save" some money. Low Income Housing Tax Credits totaled $142 million in 2010, the largest of the 61 tax credits.

* While General Revenue (GR) has grown 14 percent since 1998 in nominal dollars, when adjusted for inflation, GR has actually declined. FY 2010 GR was nearly $1 billion lower than it was in FY 2000.

- Eliminate or modify the carry back or carry forward provisions of tax credits (the ability to claim tax credits for previous years' taxes paid, or carry unclaimed tax credits into future years) to achieve greater budget certainty in a given year.
- Develop standards to monitor projects for reasonable cost per unit or per beneficiary.
- Enact and enforce statutory clawback requirements if the recipient of a tax credit does not meet compliance standards regarding performance or program requirements.
- Establish limits on "stacking" multiple tax credits in the same project.
- Replace various economic development tax credits with one flexible, unified program.
- Urge Congress to pass legislation that limits state-to-state competition regarding tax incentives that pit one state against another.

The Commission was unable to reach consensus on one global issue. The Commission agreed that Economic Development Tax Credits should generate a positive return on investment, as measured by the REMI model. However, members could not reach agreement on whether the REMI model was appropriate to measure the return on investment of tax credits that are designed to achieve social benefits (such as the Food Pantry or Children in Crisis Tax Credits) or to achieve both economic and social benefits (such as Historic Preservation Tax Credits and Low Income Housing Tax Credits).

Specific Tax Credits

The Commission made many suggestions regarding specific tax credits. To read the full report, visit http://tcrc.mo.gov. Some highlights of the recommendations are included below.

Historic Preservation Tax Credits

Historic Preservation Tax Credits account for the third largest share of credits, with $108 million in Historic Preservation Tax Credits redeemed in FY2010. Specific recommendations regarding these include:

- Lower the cap from $140 million to $75 million per year. The current cap was set in 2009. Owner-occupied residential projects have a per-project cap of $275,000 in tax credits. Any project other than these owner-occupied residential projects receiving less than $275,000 in tax credits are currently exempt from the overall program's cap. The commission recommends that all credits after July 1, 2011 be subject to the cap of $75 million (except those described in the bullet below).
- Prohibit stacking of Historic Preservation and Low Income Housing Tax Credits except in projects using tax-exempt bonds. In these instances, the Historic Preservation Tax Credits would not be subject to the $75 million cap.
- Ensure changes to the program's cap do no harm to projects currently underway.
- Prohibit Historic Preservation Credits from being stacked with Neighborhood Preservation Tax Credits.
- Issue tax credits on qualified rehabilitation expenses that have been paid, rather than incurred.

Property Tax Credit / Senior Citizens' Circuit Breaker Tax Credit

$119 million in Property Tax Credits, otherwise known as the Senior Citizens' Circuit Breaker Tax Credits, were redeemed in FY2010, making it the state's second largest credit. The credit may be claimed by senior citizens, veterans with a disability, persons with 100 percent disability, and certain widows and widowers. The tax credit phases out as adjusted income rises above

$14,300, to a lid of $30,000 for homeowners and $27,500 for renters. The Commission recommends that renters not be allowed to claim this benefit.

Social and Contribution Tax Credits

These credits, intended to serve vulnerable Missourians, are generally used to provide an incentive for private donations to certain organizations that provide services to those Missourians. The Commission recommends that the state:

- Lower the value of all these tax credits. Current values range from 70 cents on each dollar donated to 30 cents on each dollar. Recommended changes would decrease the 70 percent credits to 50 percent, and the 50 percent credits to 35 percent. The 30 percent rate would not be lowered.
- Allow all tax credits to be transferable (sold) if the donor does not have a Missouri tax liability.
- Reduce the value of transferred credits (e.g., a credit could be transferred at 90 percent of its value, so a 50 percent credit would have a value of 45 percent after being transferred).
- Eliminate or raise any "per contribution" caps.
- Allow underutilized programs to sunset (specifically, the Family Development Account Tax Credit, Healthcare Access Fund, the Commercial and Residential Disabled Access Tax Credit, and the Public Safety Surviving Spouse Tax Credit).
- Restrict the Special Needs Adoption and Children in Crisis Tax Credit to make international adoptions an ineligible expense.
- Increase the per donor limit to $10,000 for food donations and $50,000 for cash donations to incentivize larger contributions.

Angel Tax Credit

The Commission recommended that the state establish a new Angel Tax Credit to address the financing gap that is an obstacle to growing new businesses within the state. The cost would be offset by eliminating the Film Tax Credit, which does not result in an adequate return on investment.

Changes to Tax Law

The Commission also offered several suggested changes to both state and federal tax laws to improve the application of existing tax credits.

Recommendations requiring federal action

- Allow a federal tax deduction for purchased tax credits.
- Enact provisions to exclude the amount realized from the sale of state tax credits from gross income in determining federal taxes.

Related to state taxes

- Make the Missouri Low Income Housing Tax Credit a transferable credit (a credit that may be sold).