Fiscal Note

BILL # HB 2736

TITLE: ~~tobacco products; distributor licenses~~ S/E: tax credits; affordable housing

SPONSOR: Toma

STATUS: As Amended by Senate APPROP

PREPARED BY: Sam Beres

Description

The bill would establish a non-refundable affordable housing tax credit that is equal to the federal low-income housing tax credit for investments in qualifying rental housing. The annual growth in the credit would be capped at $10.0 million per year.

Estimated Impact

The bill is estimated to reduce General Fund revenues by $(10.0) million in FY 2022. This reduction reflects use of the first full year of credits which are allocated in tax year (TY) 2020 and claimed in TY 2021. The revenue loss would gradually increase to an annual impact of $(93.3) million in FY 2031, which reflects the use of 10 installments of credits allocated from TY 2020 through TY 2029. *Table 1* displays the estimated impact by year and by tax category. As discussed in the *Analysis* section, some credits available to corporate income taxpayers are projected to go unused in FY 2030 and FY 2031, due to insufficient tax liability.

The timing of the fiscal impact will depend on multiple factors. The JLBC Staff's estimate assumes that:

- The Department of Housing (DOH) will have rules and procedures in place in time to allocate state credits during the spring of 2020. If these procedures are not in place in time, then state credits may not begin to be allocated until as late as the spring of 2021.
- Any credits allocated in a given year will not be claimed until the following tax year. Credits cannot be claimed until the project is completed and placed into service. For example, the JLBC Staff assumes that credits issued in calendar year 2020 will be claimed in TY 2021, and thus would impact FY 2022 revenues.

DOH estimates that the credit would cost $10.0 million in its first full year of being claimed. The department expects the cost of the credit would increase to $100.0 million by the tenth full-year of credit claims. Unlike the JLBC Staff, DOH's analysis assumes that sufficient tax liability will exist to utilize the full amount of the tax credits in each year.

Table 1

Fiscal Impact Summary
($ in Millions)

Year	Corporate Income Tax	Individual Income Tax	Insurance Premium Tax	Total [1/]
FY 2022	$(7.8)	$(0.8)	$(1.5)	$(10.0)
FY 2023	(15.5)	(1.5)	(3.0)	(20.0)
FY 2024	(23.3)	(2.3)	(4.4)	(30.0)
FY 2025	(31.0)	(3.1)	(5.9)	(40.0)
FY 2026	(38.8)	(3.9)	(7.4)	(50.0)
FY 2027	(46.5)	(4.6)	(8.9)	(60.0)
FY 2028	(54.3)	(5.4)	(10.4)	(70.0)
FY 2029	(62.0)	(6.2)	(11.8)	(80.0)
FY 2030	(67.5)	(6.9)	(13.3)	(87.7)
FY 2031	(70.8)	(7.7)	(14.8)	(93.3)

1/ Amounts may not add to totals due to rounding.

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DOH expects that any costs incurred in administering this program would be covered by fees charged for issuing the credits.

Analysis

Federal Credit Background

The federal government provides Arizona's DOH an allotment of federal Low-Income Housing Tax Credits (LIHTC). The agency allocates the credits to developers and investors of qualifying rental housing projects, which may use the credits to reduce their federal corporate income and individual income tax liability. The credits administered by DOH are intended to offset 70% of a project's cost over a 10-year period. DOH expects to allocate approximately $18.0 million of LIHTC for 2019, which may be taken for 10 consecutive years (total of $180 million in credits over 10 years). The federal allotment provided to the state is increased annually by formula adjustments for inflation and population growth. DOH allocates these credits during the spring of each year.

A maximum of 20% of the state tax credits created under this bill would be eligible to be awarded to projects utilizing tax-exempt financing. According to data from the U.S Department of Housing and Urban Development (HUD), approximately 10% of Arizona LIHTC projects over the past 10 years have utilized tax exempt bond financing. Based on this data, the JLBC Staff does not expect the 20% limit to affect demand for the state tax credits.

Availability of State Credits

HB 2736 would permit investors an amount of state affordable housing tax credits that is equal to the amount of federal LIHTC issued for Arizona projects that are placed into service after June 30, 2020. The annual amount of credits that could be issued by DOH would be capped at $10.0 million for a given tax year. Given that expected 2019 issuances already exceed this cap, the JLBC Staff anticipates that this cap will be reached in TY 2020 and each year thereafter. Issuing the full $10.0 million of tax credits in TY 2020 would require DOH to have adequate rules and procedures in place by the spring of 2020. Any credits issued in TY 2020 would not be eligible to be claimed against tax liability until the project was completed and placed into service. According to the DOH, project completion typically takes 18-24 months.

Under the bill, taxpayers would receive an estimated $10.0 million in state credits available to offset corporate and individual income and insurance premium tax liability in FY 2022. That amount reflects the first installment of credits that are issued in TY 2020, and assumes the projects are placed in service during TY 2021. The total amount of available credits under the bill would gradually increase to $100.0 million in FY 2031, which consists of 10 credit installments for projects placed in service in TY 2020 through TY 2029.

Using IRS data of the federal LIHTC the JLBC Staff projects that 77.5% of available state credits will be received by corporate income taxpayers, 14.8% by insurance premium taxpayers and 7.7% by individual income taxpayers. Of the $100.0 million in available credits in FY 2031, $77.5 million is specific to corporate income tax, $14.8 million to insurance premium tax, and $7.7 million to individual income tax.

Impact of State Credit Use

The impact of the bill depends on the extent that taxpayers have tax liability to offset with available credits. While all estimated available credits claimed for insurance premium and individual income taxpayers are expected to be used, a portion of corporate income tax credits are expected to exceed liability and go unused.

Using IRS data, the JLBC Staff estimate that 89% of federal corporate LIHTC in TY 2013 were claimed by taxpayers in finance or holding company industries (excluding insurance corporations). Businesses in those industries accounted for 10% of federal corporate taxable income in TY 2013. Based on that estimate, the JLBC Staff made a simplifying assumption that corporations that would earn the bill's credit pay no more than 10% of current state corporate income tax revenues.

Under the Baseline, corporate income tax revenue collections are projected to be $460.3 million in FY 2022. IHS Markit, a forecasting firm, projects Arizona Gross State Product will grow by an average of 4.9% a year from 2022 to 2030. Applying IHS Markit's 4.9% rate of growth, the JLBC Staff project state corporate income tax collections will grow to $708.0 million by FY 2031 (*see Table 2*).

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The amount of credits available to corporations are projected to equal $7.8 million in FY 2022 and grow to $62.0 million in FY 2029. Corporate taxpayers are projected to use the full amount of available credits in those years, as projected credit amounts are less than the taxpayers' estimated corporate tax liability of $46.0 million in FY 2022 and $64.3 million in FY 2029. In FY 2030 and FY 2031, the amount of credits used by corporations is expected to be limited by the taxpayer's liability. For example, while corporations would have $77.5 million in available credits in FY 2031, they are projected to use $70.8 million to reduce their tax liability to $0.

Table 2

Summary of Available and Used Corporate Credits Under Bill

($ in Millions)

Year	Baseline CIT Revenues	10% of Baseline Collections	Available Credits	Used Credits
FY 2022	$460.3	$46.0	$7.8	$7.8
FY 2023	482.9	48.3	15.5	15.5
FY 2024	506.5	50.7	23.3	23.3
FY 2025	531.3	53.1	31.0	31.0
FY 2026	557.4	55.7	38.8	38.8
FY 2027	584.7	58.5	46.5	46.5
FY 2028	613.3	61.3	54.3	54.3
FY 2029	643.4	64.3	62.0	62.0
FY 2030	674.9	67.5	69.8	67.5
FY 2031	708.0	70.8	77.5	70.8

Under projected use of all credits, the bill is estimated to reduce General Fund revenues by $(10.0) million in FY 2022. This reduction reflects use of the first installment of credits that are received during TY 2020. The revenue loss would gradually increase to $(93.3) million in FY 2031, which reflects use of 10 installments of credits earned from TY 2020 through TY 2029. The estimated revenue reduction by year and by tax category is summarized in *Table 1*, above.

DOH estimates that the bill would reduce revenues by $(10.0) million during the first full year of credit claims. That cost would grow to $(100.0) million in the tenth year. This estimate is greater than the JLBC Staff's because it assumes that there will be sufficient tax liability to utilize the full credit amounts in each year.

DOH is uncertain whether it can have rules and procedures in place in time to issue credits for TY 2020. If DOH were not ready to administer the credit in the spring of 2020 (the time period in which it will administer the existing federal tax credit), then credits will not be issued until TY 2021. If that were to occur, the fiscal impact of the bill would likely not begin until FY 2023.

Local Government Impact

Each year, incorporated cities and towns receive 15% of income tax collections from 2 years prior. The bill would decrease local government distributions by $(1.5) million in FY 2024, an amount which gradually increases to $(14.0) million in FY 2033.

3/27/19