Finance & Tax Committee

Thursday, January 27, 2011
1:15 p.m.
17 HOB

MEETING PACKET

Dean Cannon
Speaker

Stephen Precourt
Chair

Finance and Tax Committee

AGENDA

January 27, 2011
1:15 p.m. – 5:00 p.m.
Morris Hall

I. Call to Order/Roll Call

II. Overview of State Debt Finance, presentation by Ben Watkins, Florida Division of Bond Finance

III. Fundamentals of the Florida Corporate Income Tax, staff presentation

IV. Chairman's Comments

V. Final Remarks and Adjournment

Overview of State Debt Finance

State of Florida

Debt Overview

Presented by

The Division of Bond Finance

House Finance and Tax Committee
January 27, 2011

Authority for State Debt

- Constitutional framework for debt
  - General Principles
    - State general obligation bonds (full faith and credit) may only be issued when approved by voters – Article VII §11(a)
  - Bonds secured by taxes may be issued when authorized by Constitutional amendment (voter approval)
    - No pledge of taxes without voter approval
  - Revenue Bonds secured by non-tax revenues may be issued without voter approval – Article VII §11(d)

Limitations on Debt

- Limits on debt imposed in various ways

  (1) Constitutional limits on individual programs

  Example: PECO – no more than 90% of gross receipts taxes for debt service – Article XII §9(a)(2)

  (2) Statutory limits

  Examples:

  Preservation 2000/Florida Forever – no more than $30 million in debt service in each year additional debt is authorized;

  Right-of-Way – no more than 7% of State Transportation Trust Fund revenues for debt service

  (3) Bond documents

  Example: Limited by enterprise revenues pledged plus additional bonds test

The Debt Affordability Analysis

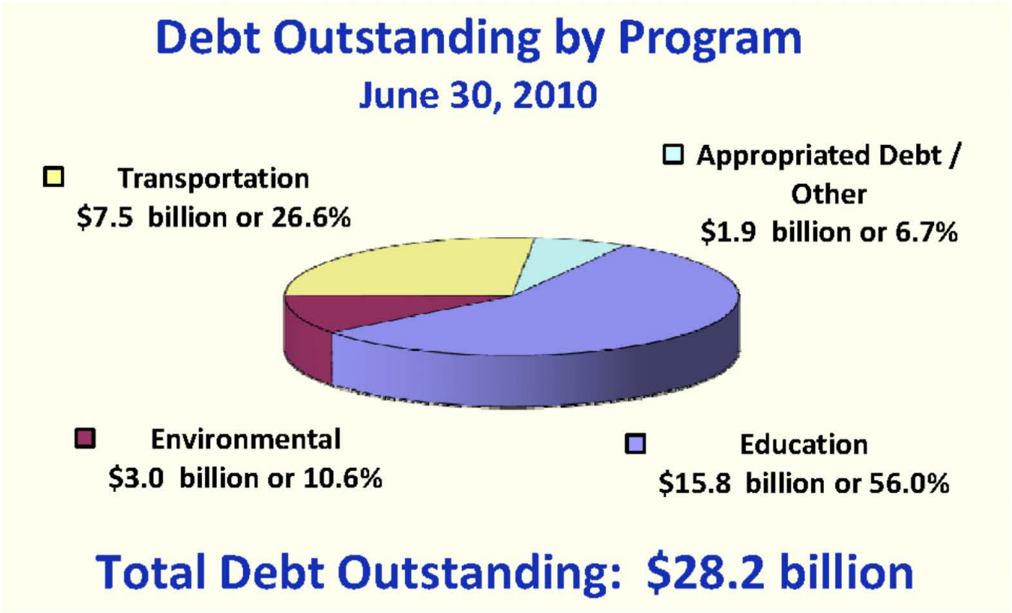
- Purpose of Debt Affordability Analysis is to Provide a Framework for Measuring, Monitoring and Managing the State’s Debt Position
- Provides Information to Assist Legislature in Formulating Capital Spending Plan
- Analytical Approach to Evaluating the State’s Debt Position
- Financial Model to Calculate Future Bonding Capacity Based on Two Variables
    1) Reasonable Borrowing Levels Measured by Debt Ratios
    2) Amount of State Revenues Available to Pay Debt Service
- Model Provides Framework for Evaluating Long-term Impact of Existing and New Financing Programs

Debt Affordability Analysis

- Calculate Total State Debt Outstanding
- Evaluate Growth in Debt and Annual Debt Service Requirements Over Last Ten Years
- Update Projections for Expected Future Debt Issuance and Revised Revenue Estimates
- Calculate Benchmark Debt Ratio Based on Expected Future Debt Issuance and Revenue Collections
- Calculate the Estimated Debt Capacity Available Based on the 6% Target and 7% Cap
- Evaluate Level of Reserves and Review Credit Ratings

State Debt Outstanding

Total Debt Outstanding: $28.2 billion

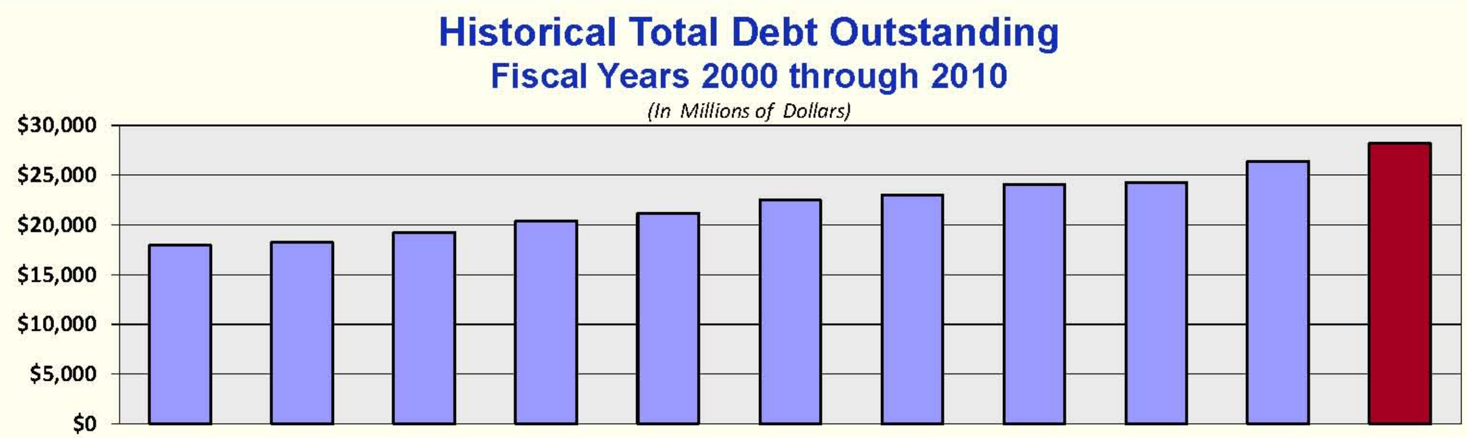


Debt Outstanding by Type as of June 30, 2010

(In Millions of Dollars)

Debt Type	Amount
Net Tax-Supported Debt	$ 23,557.3
Self-Supporting Debt	4,610.5
Total State Debt Outstanding	$ 28,167.8

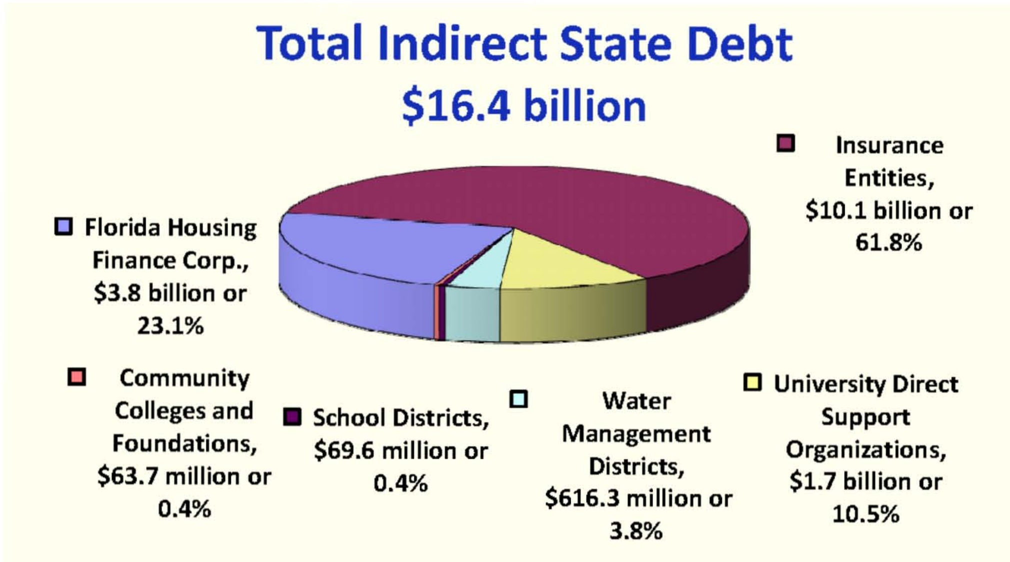
Growth in Debt Outstanding



	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Debt Outstanding	$17,958.3	$18,267.4	$19,216.2	$20,380.3	$21,196.9	$22,461.7	$23,025.1	$24,092.3	$24,262.6	$26,408.7	$28,167.8
Percentage Change	-	1.7%	5.2%	6.1%	4.0%	6.0%	2.5%	4.6%	0.7%	8.8%	6.7%

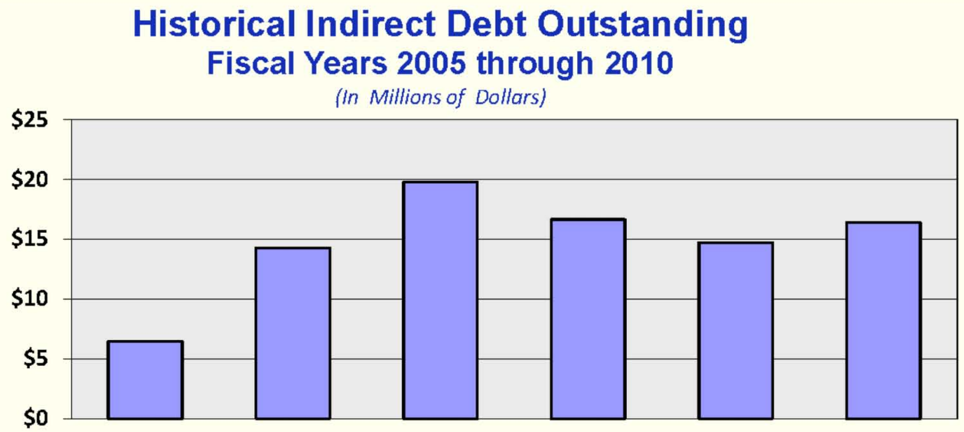
- Over the last ten-years debt outstanding increased $10.2 billion from $18 billion in 2000 to $28.2 billion in 2010
- $3.1 billion of debt issued in 2010
- Net increase in debt outstanding for 2010 was $1.8 billion; increase is 80% more than the ten-year average annual increase
- Net tax-supported debt increased $1.2 billion
  - Single largest increase $543 million for Public/Private Partnership (P3) agreement related to Port of Miami Tunnel project

Indirect Debt



- Indirect debt is either not secured by traditional State revenues or is primary obligation of another legal entity
- Insurance entities account for $10.1 billion or 62% of the indirect debt
  - Florida Hurricane Catastrophe Fund Financing Corporation, $5.6 billion
  - Citizens Property Insurance Corporation, $4.5 billion
- Florida Housing Finance Corporation accounts for $3.8 billion or 23%
- University Direct Support Organizations make up 10.5% or $1.7 billion of the total

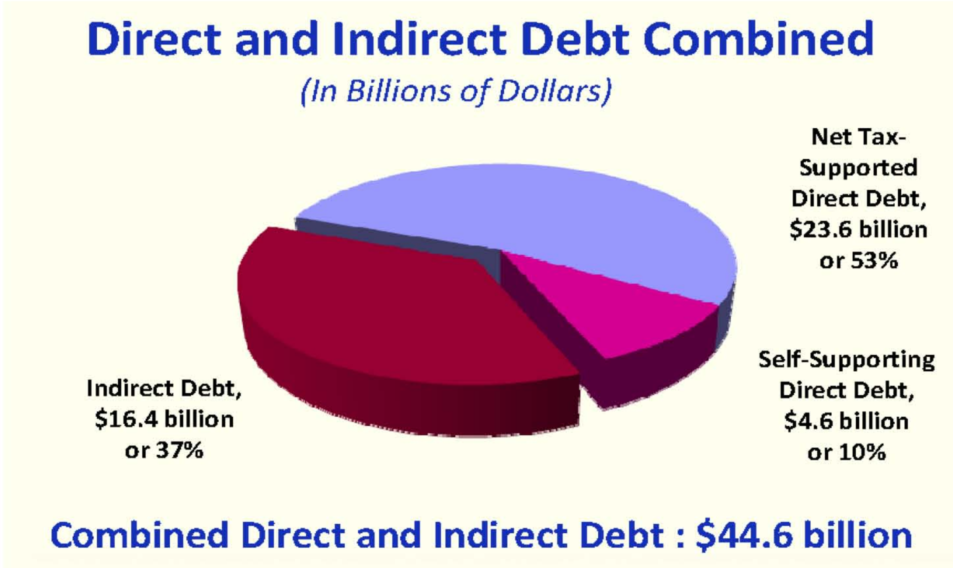
Growth in Indirect Debt



	2005	2006	2007	2008	2009	2010
Indirect Debt	$6.5	$14.3	$19.8	$16.6	$14.7	$16.4
Percentage Change	-	120.0%	38.5%	(15.8)%	(11.5)%	11.4%

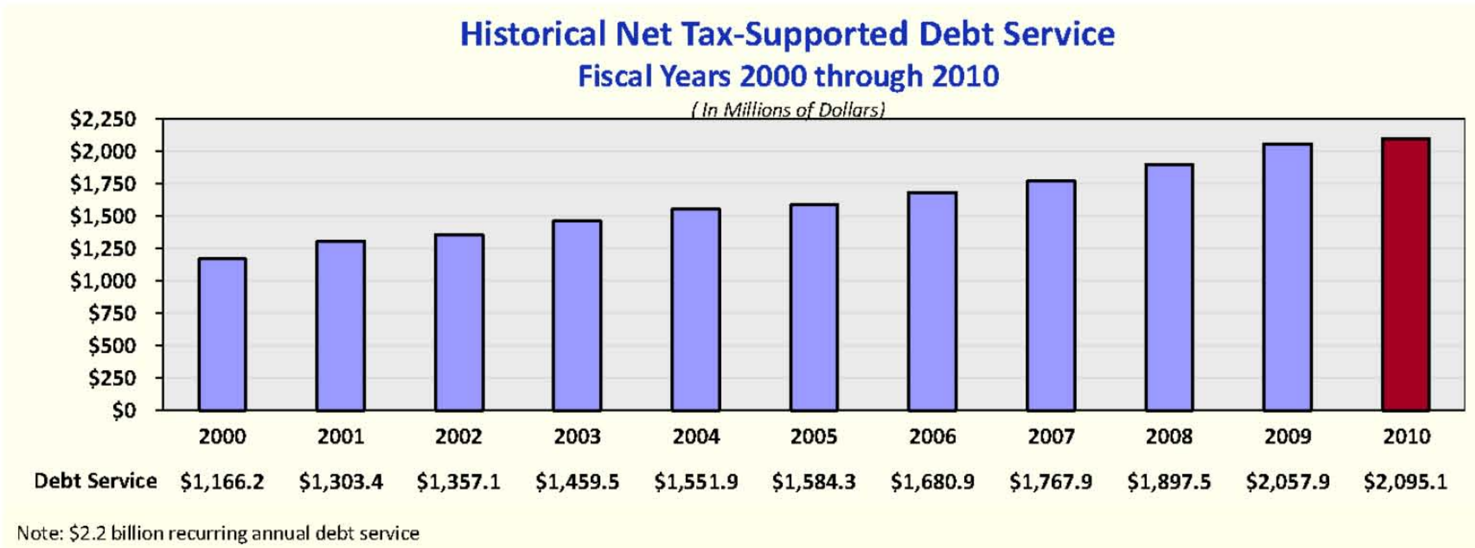
- Indirect debt increased $10 billion over the last five years from $6.5 billion in 2005 to $16.4 billion in 2010
- Insurance entity borrowing for liquidity and claims paying purposes
- Increase primarily due to liquidity financings by the insurance entities
  - Liquidity financing debt outstanding at June 30, 2010 was $7.1 billion
    - Florida Hurricane Catastrophe Fund Financing Corporation, $3.5 billion
    - Citizens Property Insurance Corporation, $3.6 billion

Direct and Indirect Debt Combined



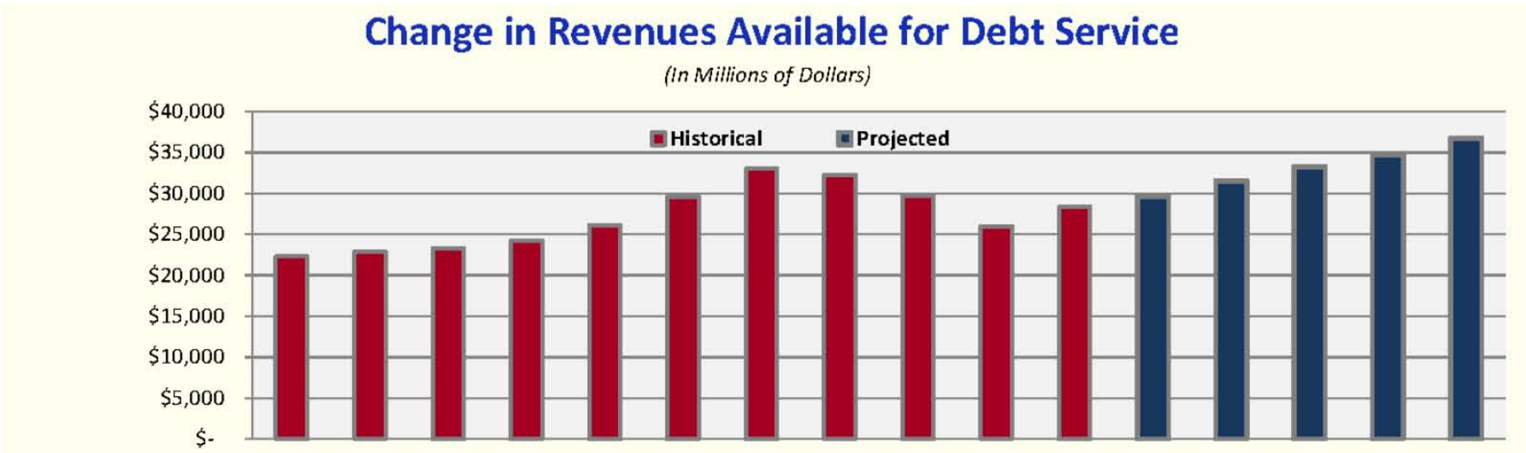
- Combined direct and indirect debt totaled $44.6 billion at June 30, 2010
- Direct debt comprises 63% of the total
    - Net tax-supported debt, 53% and self-supporting debt, 10%
- Indirect debt represents 37% of the combined debt
- While not direct debt of the State, rating agencies are considering the impact of potential hurricane costs and insurance entity assessments as a factor which could impact the State's rating

Growth in Annual Debt Service



- Debt service for net tax-supported debt has nearly doubled over the last ten years increasing from $1.2 billion in 2000 to $2.1 billion in 2010
- 2010 debt service was $37.2 million more than 2009, but would have been $169.6 million more, if adjusted for annualized debt service for 2010 issuances
- Debt service on existing outstanding debt increases to $2.3 billion in 2013
- Payments do not begin on $1.8 billion P3 obligations until after the completion of the projects in 2013 and 2014 delaying the impact of the required payments

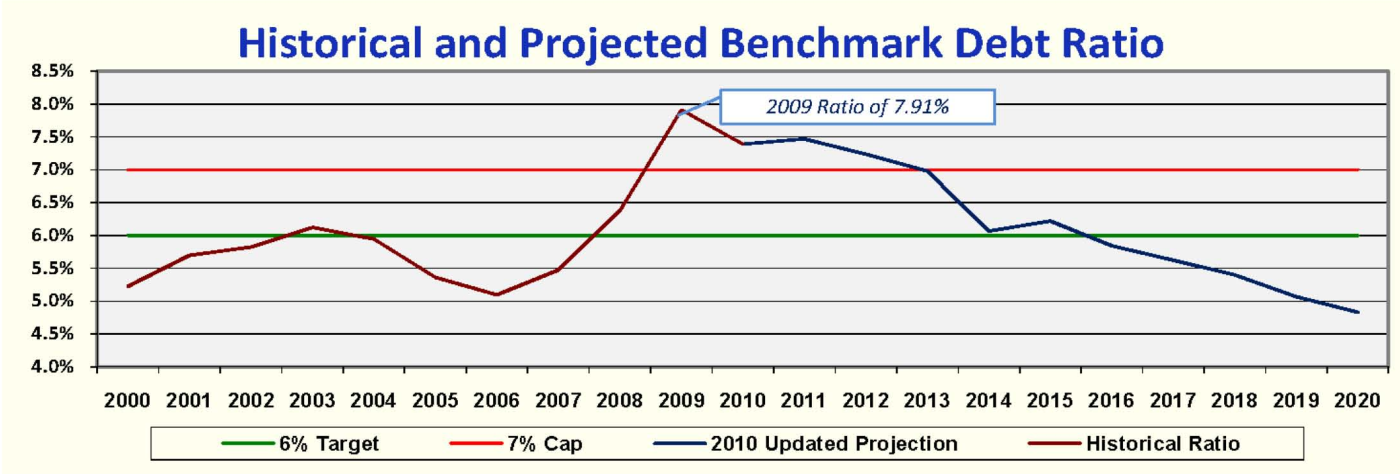
Revenues Available for Debt Service



January 2011 Update	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Available Revenues	$ 22.3	$ 22.9	$ 23.3	$ 24.2	$ 26.1	$ 29.5	$ 33.0	$ 32.3	$ 29.7	$ 26.0	$ 28.3	$ 29.6	$ 31.5	$ 33.2	$ 34.7	$ 36.7

- Revenues available for debt service includes general revenues and specific revenues pledged to various bond programs
- Significant revenue declines in 2007 through 2009 due to the weak economy
- In 2010 revenues were virtually on estimate with no major adjustments in short-term estimates
- 2010 revenues were $2.3 billion over 2009 but, $1.8 billion of increase due to the addition of a revenue source and $500 million from organic growth in revenues
- Projected revenues are based on the December 2010 Revenue Conference results

Projected Benchmark Debt Ratio

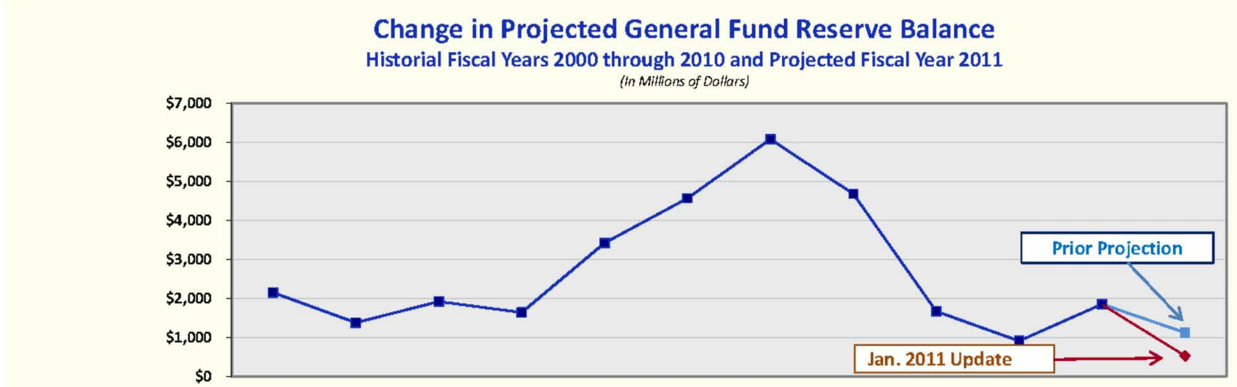


Benchmark Ratio Projection

	2010 Actual	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
2010 Updated Projection	7.39%	7.47%	7.24%	6.98%	6.06%	6.22%	5.84%	5.62%	5.40%	5.07%	4.83%

- Benchmark debt ratio is debt service as percentage of available revenues
- Benchmark debt ratio improved to 7.39% for Fiscal Year 2010
- Benchmark debt ratio is projected to exceed the 7% Cap through 2012
- Significant improvement in the benchmark debt ratio in 2010 is due to adding revenues to base and only a partial year debt service for 2010 issuances
- Projected improvement in the benchmark debt ratio is largely dependent on realizing projected revenue growth

General Fund Reserves



General Fund Reserves	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
2010 Debt Affordability	$ 2,155.9	$ 1,382.7	$ 1,925.1	$ 1,641.3	$ 3,423.6	$ 4,569.8	$ 6,081.2	$ 4,682.1	$ 1,674.6	$ 912.7	$ 1,854.5	$ 1,128.2
January 2011 Update												$ 530.5
Reserves as % of Revenues	11.5%	7.2%	10.0%	8.2%	15.7%	18.3%	22.5%	17.7%	6.9%	4.3%	8.6%	2.4%

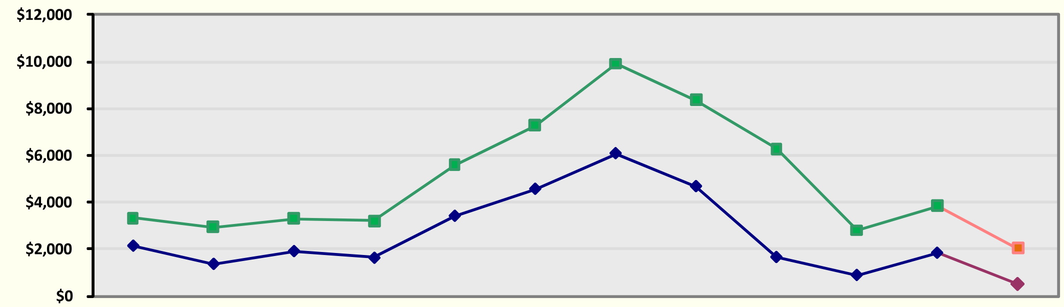
- General Fund reserves accumulated from 2003 through 2006 to an unprecedented high of 22.5% of general revenues
- Reserves were used during 2007 through 2009 to offset spending reductions due to the decline in revenues
- Fiscal Year 2010 ended with increased General Fund reserves of $1.9 billion or 8.6% of general revenues which is considered good by rating agency guidelines
- General Fund Reserves are projected to be down to $531 million or 2.4% of general revenues at the end of the current fiscal year
- Adequate reserves are critical in providing financial flexibility to respond to changes in the economic environment

Total Reserves Available

General Fund and Trust Fund Reserve Balances

Historial Fiscal Years 2000 through 2010 and Projected Fiscal Year 2011

(In Millions of Dollars)



	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011[1]
General Fund Reserves	$ 2,155.9	$ 1,382.7	$ 1,925.1	$ 1,641.3	$ 3,423.6	$ 4,569.8	$ 6,081.2	$ 4,682.1	$ 1,674.6	$ 912.7	$ 1,854.5	$ 530.5
Reserves as % of Revenues	11.5%	7.2%	10.0%	8.2%	15.7%	18.3%	22.5%	17.7%	6.9%	4.3%	8.6%	2.4%
Trust Fund Reserves	$ 1,181.0	$ 1,561.0	$ 1,393.0	$ 1,571.0	$ 2,170.5	$ 2,714.0	$ 3,831.5	$ 3,684.7	$ 4,612.0	$ 1,890.0	$ 1,993.0	$ 1,526.0
General Fund and Trust Fund Reserves	$ 3,336.9	$ 2,943.7	$ 3,318.1	$ 3,212.3	$ 5,594.1	$ 7,283.8	$ 9,912.7	$ 8,366.8	$ 6,286.6	$ 2,802.7	$ 3,847.5	$ 2,056.5
Reserves as % of Revenues	17.7%	15.3%	17.2%	16.1%	25.6%	29.1%	36.6%	31.7%	26.1%	13.3%	17.9%	9.2%

[1] Projected

- Budgetary practices identify trust fund balances that are available and can be used for other purposes
- Legislature has routinely permitted trust fund balances to be used as a source of revenues in the General Fund budget
- Total reserves, including trust fund balances, were $3.8 billion or 17.9% of general revenues at June 30, 2010
- Current fiscal year budget contemplates use of reserves and, therefore, reserves at the end of 2011 are expected to decline to $2.1 billion or 9.2% of general revenues

Credit Rating Considerations

- Rating analysis focuses on five primary areas
  - Governance Factors
  - Financial Management Factors
  - Budgetary Performance Factors
  - Economic Factors
  - Debt and Liability Profile Factors

State Credit Ratings

Ratings are an important indicator in credit markets and influence the interest rates that the State pays

State of Florida
General Obligation Credit Ratings

	Rating	Outlook
Standard & Poor's	AAA	Negative
Fitch Ratings	AAA	Negative
Moody's Investor Service	Aa1	Stable

Credit Strengths:

- Conservative budget and financial management
- Swift response to budget pressure from declining revenues
- Adequate reserves
- Moderate debt burden with clear guidelines
- Strong pension funding ratios and limited OPEB liability

Challenges:

- Weaker economy and declining revenues
- Budgetary pressure for addressing the drop-off of federal stimulus moneys included in the budget
- Reliance on one-time revenues to balance the budget
- Restoring and maintaining adequate reserves

State ratings remain vulnerable and rating agencies will be carefully monitoring future economic and budgetary developments

Conclusion

- At June 30, 2010, State direct debt of $28.2 billion and indirect debt of $16.4 billion
- Direct debt issued in 2010 totaled $3.1 billion
- Indirect debt and obligations related to Public/Private Partnerships are becoming a more significant factor in the State's overall debt profile
- Recurring annual debt service requirements on existing obligations are $2.2 billion
- Benchmark debt ratio of 7.39% is still in excess of 7% policy cap
- Projected improvement in benchmark debt ratio largely dependent on forecasted growth in revenues
- General Fund reserves at June 30, 2010 of $1.9 billion are up from 2009 but are projected to decrease to $531 million during the current fiscal year
- Total reserves, including trust fund balances, were $3.8 billion at June 30, 2010 and are expected to decline to $2.1 billion during the current fiscal year
- State ratings are very strong (AAA, AAA, Aa1) but are vulnerable to economic conditions and budgetary challenges

Florida Corporate Income Tax

Finance and Tax Committee

January 27, 2010

FLORIDA CORPORATE INCOME TAX

OUTLINE

- The Big Picture
- Six Steps to Calculating the Tax

CORPORATE INCOME TAX: BIG PICTURE

- What is the Tax?
  - First enacted in 1971, effective January 1, 1972
  - 5.5% of Net Income *Earned in Florida* by certain corporations
  - As such, it is a *tax on the earnings of capital*

CORPORATE INCOME TAX: BIG PICTURE

- How much is Paid?
  - $2 billion in FY 2011-12
  - All to General Revenue
  - 9.1% of GR revenue sources
  - A volatile revenue source
  - Declining economic presence

CORPORATE INCOME TAX: BIG PICTURE

- Who Pays the Tax?
  - Only C-corporations with *"nexus"* in Florida
  - Most Florida businesses *do not pay:*

Corporate Income Tax Filers (2008)	192,843
Active Business Entities (Jan. 2010)	
All For-Profit Corporations	820,401
Limited Partnerships	21,481
Limited Liability Companies	499,143
General Partnerships	12,978

CORPORATE INCOME TAX: BIG PICTURE

- Who Pays the Tax? (cont'd)
  - Most C-Corporations *do not pay:*

Florida Corporate Income Tax, Number of Returns, 2008 Tax Year

With Tax Due, 30,880 , 16%

No Tax Due, 161,963 , 84%

CORPORATE INCOME TAX: BIG PICTURE

- Who Pays the Tax? (cont'd)
  - Some Sectors of the Economy Pay more:

Florida Corporate Income Tax, 2008 Tax Due Selected Economic Sectors		
	Tax (mil $)	% of Total
Finance & Insurance	$352	23%
Retail Trade	$226	15%
Manufacturing	$178	12%
Management of Companies & Enterprises	$143	9%
Information	$125	8%
Wholesale Trade	$122	8%
		75%

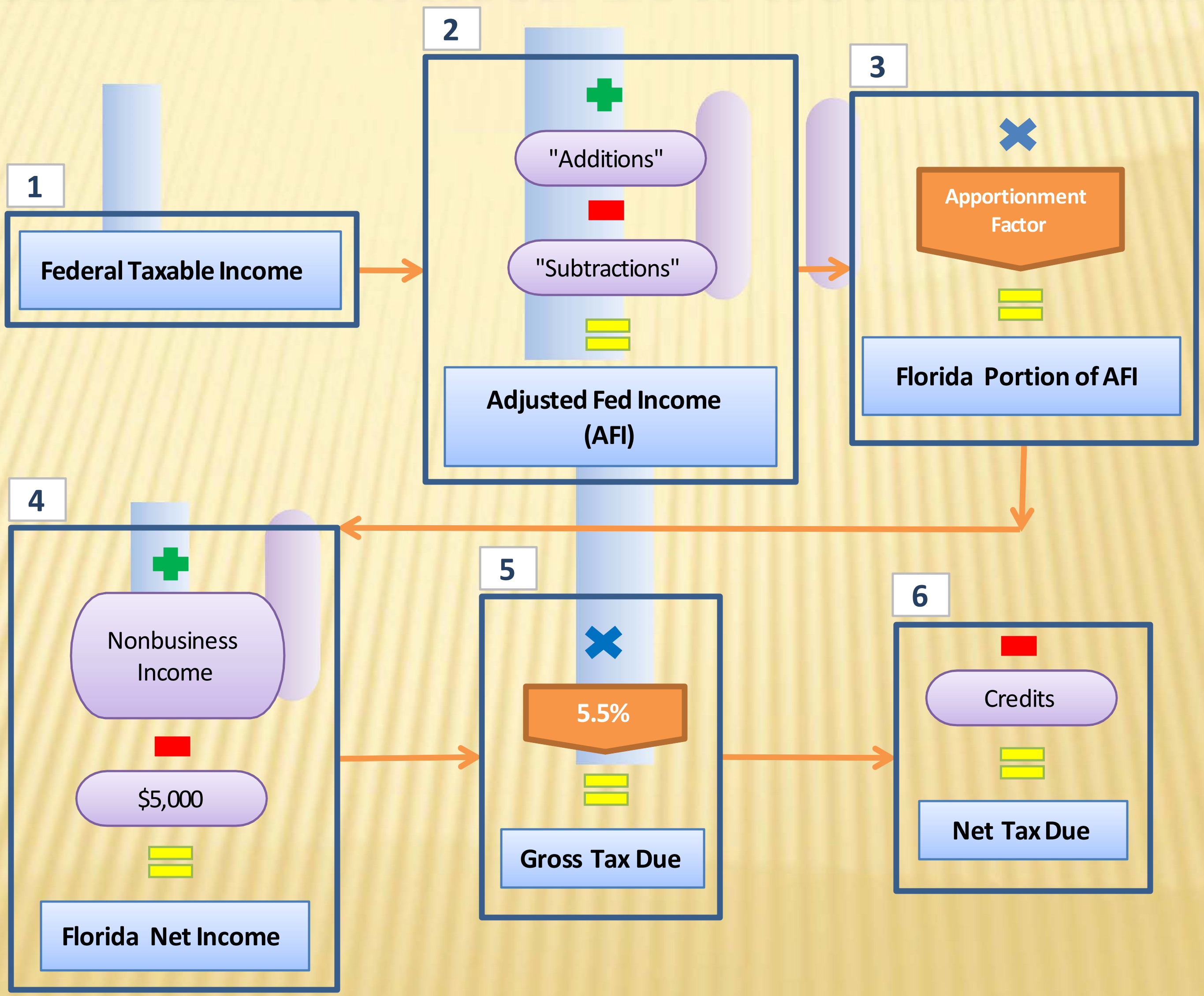
CORPORATE INCOME TAX: BIG PICTURE

- When is the Tax Paid?
  - *Annual Tax,* depends on company's tax year
  - *Four estimated payments are made throughout the year*
  - *True-up after tax year is over*

CORPORATE INCOME TAX: BIG PICTURE

- How Does Florida Compare to Other States?
  - Only Nevada, South Dakota, Washington (state) and Wyoming do not impose some form of corporate income or franchise tax.
  - Most levying states have flat tax rates. Rates range from 4.63 percent to 9.99 percent.
  - Sixteen states use graduated rates. Most ranges fall completely between 1.0 and 9.99 percent. Iowa goes up to a 12 percent maximum rate.

CORPORATE INCOME TAX CALCULATION



STEP 1: THE STARTING POINT

- Florida tax calculations start with *Federal Taxable Income*
- Who’s taxable income?
  - Single companies?
    - This is the general rule
  - Groups of companies?
    - Related companies can elect to file as a consolidated group

STEP 2: ADJUSTMENTS TO FED INCOME

- There are a number of adjustments required to be made to the federal taxable income starting point to determine Florida's adjusted federal taxable income.
- Additions to taxable income include:
  - Federal deductions for state and local taxes
  - To the extent expenses related to such credits were deductible for federal purposes:
    - Credits for contributions to nonprofit scholarship-funding organizations
    - Entertainment industry financial incentive program credits
- Subtractions from taxable income include:
  - Certain foreign source dividends
  - Certain foreign source income

STEP 3: DETERMINE FLORIDA'S SHARE

- Apportionment is how you determine the portion of adjusted federal income that is taxable in a given state
  - Florida Uses a Three Factor Apportionment formula for most taxpayers:
    - Payroll (25%)
    - Property (25%)
    - Sales (50%)

STEP 4: FLORIDA NET INCOME

- After apportionment, *Florida net income* is calculated by adding "allocated nonbusiness income," then subtracting a $5,000 exemption.
- Nonbusiness income = certain types of income not arising from transactions and activities in the regular course of the taxpayer's trade or business.
- Example: A taxpayer is engaged in a multistate glass manufacturing business.
  - Holds a portfolio of stock and interest-bearing securities, the acquisition and holding of which are unrelated to the manufacturing business.
  - The dividends and interest income received are nonbusiness income.

STEP 5: APPLY THE TAX RATE

- *Gross tax due* is calculated by multiplying Florida net income by the corporate income tax rate of 5.5%.

STEP 6: NET OUT THE CREDITS

- The final step to determine the *net tax due*, is to subtract any allowable credits from gross tax due. Such credits include:
  - Entertainment industry tax credit
  - Nonprofit scholarship funding organization tax credit
  - Enterprise Zone Jobs tax credit

Q & A

Chairman's Comments

Finance and Tax Committee Goals

1. Avoid Raising Taxes or Fees
2. Pursue broad-based tax relief for Florida's families and businesses
3. Encourage businesses to locate and expand in Florida
4. Simplify the current tax system