

SUBJECT: Reducing the interest rate paid on certain tax refunds

COMMITTEE: Ways and Means — favorable, without amendment

VOTE: 5 ayes — J. Keffer, Edwards, Grusendorf, Paxton, Ritter

0 nays

4 absent — Villarreal, Luna, Smithee, Woolley

SENATE VOTE: On final passage, April 14 — 31-0, on Local and Uncontested Calendar

WITNESSES: No public hearing

BACKGROUND: Under Tax Code, ch. 111.064, the state pays interest on tax refunds at a rate equal to the prime rate, which is published in the *Wall Street Journal* on the first business day of the calendar year, plus 1 percent. Interest on tax overpayments begins to collect 60 days after the date of the payment and continues to collect until the tax is refunded or until 10 days before a refund warrant is served.

A credit taken by a taxpayer on a future tax return does not accrue interest. No interest accrues for refund claims made during a reporting period prior to January 1, 2000.

All warrants for interest payments are drawn against the fund or account into which the erroneously paid tax was deposited. No interest is applied to amounts paid to the comptroller for unclaimed property under Property Code, Title 6 or through a cooperative agreement with another state under Tax Code, sec. 153.017.

DIGEST: SB 1570 would set the interest rate on tax refunds claimed on or after September 1, 2005, and granted for a report period due on or after January 1, 2000, at the lower of:

- the average rate of interest earned on deposits in the state treasury;
or
- the prime rate, plus 1 percent.

The interest rate paid on taxes that were submitted in protest still would accrue interest at the prime rate, plus 1 percent. The bill also provides that refunds, regardless of the date claimed, for a report period due before January 1, 2000, would not accrue interest.

The bill would take effect September 1, 2005.

**SUPPORTERS
SAY:**

SB 1570 would result in savings to the state while implementing a fair and sensible policy governing interest on tax refunds. The interest rate set for tax refunds is more than 3 percent higher than the rate of return on deposits in the state treasury. The current prime rate is 4.25 percent, so the rate on tax refunds is 5.25 percent, while the rate of return on deposits in the state treasury is 2 percent. According to the fiscal note, SB 1570 would save the state approximately \$21.8 million in general revenue-related funds in fiscal 2006-07.

The bill would not reduce interest on refunds to taxpayers who pay under protest. Taxpayers pay protest payments when they make tax payments but claim the tax legally is not required. Because these tax payers remit their payments, under protest and on time, the interest rates on their refunds would not change.

The bill would apply to interest rates on refunds of *voluntary* overpayments. Often times, taxes are voluntarily overpaid when a tax-exempt organization pays sales tax on purchases from which it otherwise would have been exempted had it provided proof of tax-exempt status at the time of the purchase. Then the taxpayer seeks a refund either from the vendor who collected the sales tax or from the comptroller. By lowering the interest rates on refunds of *voluntary* overpayments, these taxpayers would not receive unfair treatment. Sales tax on their purchases still would be exempt either upon making purchases or through the refund process.

**OPPONENTS
SAY:**

It is only fair that the state pay interest to taxpayers when it does not issue refunds or credits due in a timely manner. The state expects taxpayers to pay interest when they are not timely in remitting taxes that are due. The interest rate provided by the bill would reduce the compensation the taxpayer received for having remitted taxes for which the taxpayer never was responsible. Taxpayers exempt from the sales tax often do not have proof of exemption readily available and are forced to pay sales tax on purchases. While waiting on their tax refunds, this bill would deny these taxpayers interest on money that rightfully belonged to them.

NOTES:

The House companion bill, HB 2636 by Isett, passed the House on May 9 on the Local, Consent, and Resolutions Calendar and has been referred to the Senate Finance Committee.

According to the fiscal note, the bill would save the state approximately \$21.8 million in general revenue-related funds in fiscal 2006-07.