LEGISLATIVE SERVICES AGENCY
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FISCAL IMPACT STATEMENT

LS 6161
BILL NUMBER: SB 126

DATE PREPARED: Nov 8, 1999
BILL AMENDED:

SUBJECT: Repeal of Inheritance Tax.

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FUNDS AFFECTED: X **GENERAL**
DEDICATED
FEDERAL

IMPACT: State & Local

STATE IMPACT	FY 2000	FY 2001	FY 2002
State Revenues			(102,525,000)
State Expenditures			7,452,000
Net Increase (Decrease)			(109,977,000)

Summary of Legislation: This bill provides that the state Inheritance Tax does not apply to property interest transfers made by a decedent who dies after June 30, 2000. It amends the Indiana Estate Tax formula and provides that the amended formula applies to property interest transfers made by a decedent who dies after June 30, 2000.

Effective Date: July 1, 2000.

Explanation of State Expenditures: This analysis relies on the State Revenue Forecast issued April 13, 1999. This forecast uses an estimate of $136.7 million in annual revenue from the Inheritance Tax and Estate Tax for FY 2000 and FY2001. The forecast also takes into account the loss of revenue which results from legislation passed in 1997 and increased the exemption for Class A beneficiaries beginning July 1, 1997.

There could be a state savings from a reduction in staff in the Inheritance Tax section. The Inheritance Tax section employs about 15 staff members at an annual cost of $290,000. Since staff members would still be needed to process returns, a specific savings due to staff reductions could not be estimated for the next biennium.

It is assumed that approximately 16,000 returns per year have been filed in recent years. It is anticipated that with the passage of this bill, beginning in FY 2002, there will be a dramatic reduction in the number of returns. Some returns will still be needed for the payment of state Estate Tax. The number of returns which will be filed each year after the elimination of the Inheritance Tax is not known.

P.L. 254-1997 provides for the Inheritance Tax replacement for the counties. This bill will impact the state General Fund as a result of the replacement. An explanation of that provision and the amount needed for replacement is described in the section on Local Revenues, below. Beginning with FY 2002, the state General Fund will experience an annual estimated expenditure of $7,452,000.

The maximum amount of county replacement for any year is $7,452,000. This is measured according the formula established by P.L. 254-1997. A copy of a spread sheet which shows the amount of guaranteed replacement for each county once the inheritance tax is completely phased out is available at the Office of Fiscal & Management Analysis.

Explanation of State Revenues: Based on forecasted revenue of $136.7 million for FY 2000, and the assumption that 10% of the revenue comes from the estate tax which is not impacted by this bill, the annual revenue loss to the state General Fund beginning with FY 2002 would be $123.03 million. **This represents the loss from inheritance tax. The net impact of this bill is described in the table below.**

While a revenue loss will occur when the Inheritance Tax is eliminated, this will be somewhat offset by revenue collected from the Indiana Estate Tax. Since the Indiana Estate Tax is based on the federal credit minus Inheritance Tax paid, the elimination of the Inheritance Tax will increase the base on which the federal credit is applied. Once the Inheritance Tax is completely eliminated, those estates for which federal tax is owed, would pay the maximum federal credit amount as Indiana Estate Tax. It is estimated that once the Inheritance Tax is completely phased out, Indiana will receive from the Estate Tax, approximately 25% of the amount of General Fund revenue which it had received from both the Inheritance Tax and Estate Tax.

Note: The federal tax change of 1997 relating to Estate and Gift Tax will negatively impact the receipt of state Estate Tax over a period of years. At least two new provisions will raise the amount of exempt assets from federal estate and gift taxation. This will negatively impact the amount of state Estate Tax collected by Indiana by a small amount. The phase in of the increase in exempt amounts is gradual (even stagnant in some years) and does not make a major jump until 2004. These early changes will have an almost imperceptible impact on the amount of state Estate Tax which is paid to Indiana. Even in 2004 (impacting state FY 2006) the impact will be relatively small. Based on the current law in Indiana, by the time the full $1,000,000 amount is phased in, Indiana will collect between $1 and $2 million less in State Estate Tax per year than under the current $600,000 limitation. The other new provision of significance will allow "qualified family-owned business interests" to be exempt from federal estate and gift taxation beginning in 1998. This change will also result in a reduction of state Estate Tax collections over a period of years.

Stated below is an estimate of the annual revenue impact on the state General Fund.

Fiscal Year	**Revenue Loss from Inheritance Tax**	**Revenue Gain From Estate Tax**	**Net Effect From Repeal**
2002	($123,030,000)	$20,505,000	($102,525,000)

Summary of State Impact: Based on the above estimates for expenditure and revenue impacts, the total annual loss to the state beginning in FY 2002, is estimated to be the following.

Fiscal Year	Net Effect	Expenditure for County Replacement	Total Effect From Tax Repeal and Replacement
2002	($102,525,000)	$7,452,000	($109,977,000)

Explanation of Local Expenditures:

Explanation of Local Revenues: P.L. 254-1997 contains a method for calculating an amount which will be used to distribute amounts to the counties which approximates the amount they have received from inheritance tax in the past.

Since most of the estates which pay tax during CY 00 will be calculating inheritance tax and state Estate Tax under the law prior to the effective date of this bill, most of the revenue retained by counties will be based on 8% of the Inheritance Tax paid. Full Inheritance Tax replacement will not be used until calendar year 2002.

The amount needed for replacement is based on the forecasted amount for the state General Fund for 2000. Total replacement for county general funds, to be paid from the state General Fund, state wide for each year beginning with FY 2002 will be approximately $7,452,000.

The maximum amount of county replacement for any year is $7,452,000. This is measured according the formula established by P.L. 254-1997. A copy of a spread sheet which shows the amount of guaranteed replacement for each county once the Inheritance Tax is completely phased out is available at the Office of Fiscal & Management Analysis.

State Agencies Affected: Department of State Revenue.

Local Agencies Affected: Counties.

Information Sources: State Revenue Forecast, April 13, 1999; Indiana Department of State Revenue, Bill Reynolds, 232-2075.