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FISCAL IMPACT STATEMENT

LS 6995 **NOTE PREPARED:** Apr 9, 2013
BILL NUMBER: HB 1544 **BILL AMENDED:** Apr 9, 2013

SUBJECT: Various Tax Matters.

FIRST AUTHOR: Rep. Turner **BILL STATUS:** 2nd Reading - 2nd House
FIRST SPONSOR: Sen. Hershman

FUNDS AFFECTED: X **GENERAL** **IMPACT:** State & Local
X **DEDICATED**
FEDERAL

Summary of Legislation: (Amended) *Abatements*: This bill amends the law regarding economic revitalization areas to:

(1) Allow a designating body to establish an abatement schedule in all cases (current law allows designating bodies to establish an alternative abatement schedule);
(2) Provide that an abatement schedule approved for a particular taxpayer before July 1, 2013, remains in effect until the abatement schedule expires under the terms of the resolution approving the taxpayer's statement of benefits;
(3) Repeal a statute authorizing enhanced abatements; and
(4) Remove references to deadline dates that have already passed.

Common Areas: The bill defines the term "common areas" for purposes of the circuit breaker credit law. It provides that for purposes of the circuit breaker credit, the land that is a common area shared by dwelling units of a building that includes two or more dwelling units is considered "residential property". (Current law limits the land eligible to be classified as "residential property" to only the area of the building footprint.)

Interest Rate: This bill specifies that if a taxpayer is entitled to a property tax refund or credit because an assessment is decreased, the interest rate on the refund is the rate established for excess tax payments by the Commissioner of the Department of State Revenue (DOR) (rather than 4%, under current law). The bill provides that: (1) the interest on property tax refunds or credits paid to a taxpayer; and (2) the interest paid by a taxpayer if an assessment is increased after a petition for review or a judicial proceeding has been pending; shall be calculated at the rate in effect for each year.

Sales Tax Zapper Penalty: The bill also imposes a Class C felony penalty for sale, purchase, installation, transfer, or possession of an automated sales suppression device ("zapper") or phantom-ware.

Indiana New Markets Job (INMJ) Tax Credit: This bill provides for an IMNJ tax credit against state taxes similar to the federal new markets tax credit. It excludes from the definition of a qualified active low-income community business a business that is primarily engaged in providing home ownership services. The bill excludes from the definition of a qualified active low-income community business a business that is primarily engaged in providing child care services, unless the business is a licensed child care center, child care home, or child care ministry that has the highest rating in the Paths to QUALITY^{tm} program.

The bill requires a qualified community development entity to pay the state a conditionally refundable fee of $500,000 and a nonrefundable application fee of $5,000 for each qualified equity investment (QEI) that the qualified community development entity seeks to have approved by the Indiana Economic Development Corporation (IEDC). It provides that a denial of an application by the IEDC does not create a private right of action for the applicant. It limits fees that may be charged to a qualified active low-income community business.

The bill provides that a QEI has to be made before January 1, 2016, to qualify for the credit. The IEDC may not approve more than $10 M in IMNJ tax credits per state fiscal year. The bill requires an annual report to the State Budget Committee by the IEDC on the credit program.

The bill provides that the IEDC is required to issue letter rulings requested by taxpayers, similar to private letter rulings issued by the Internal Revenue Service at the federal level, regarding the IMNJ tax credit.

Paths to QUALITY^{tm} Program: The bill establishes the Paths to QUALITY^{tm} voluntary child care rating system program. The bill requires the Division of Family Resources to adopt rules to administer the program.

Homestead Deductions: The bill allows an individual to claim a standard deduction for a homestead for a particular assessment date (and to become entitled to the supplemental standard deduction and the 1% circuit-breaker cap) even if on that assessment date the property on which the homestead is currently located was vacant land or the construction of the dwelling that constitutes the homestead was not completed.

Effective Date: (Amended) Upon passage; January 1, 2013 (retroactive); March 1, 2013 (retroactive); July 1, 2013; January 1, 2014.

Explanation of State Expenditures: *Sales Tax Zapper Penalty*: A Class C felony is punishable by a prison term ranging from two to eight years depending upon mitigating and aggravating circumstances. Assuming offenders can be housed in existing facilities with no additional staff, the marginal cost for medical care, food, and clothing is approximately $3,234 annually, or $8.86 daily, per prisoner. However, any additional expenditures are likely to be small. The average length of stay in Department of Correction (DOC) facilities for all Class C felony offenders is approximately two years.

(Revised) *Department of State Revenue (DOR):* The DOR will incur some administrative expenses relating to the revision of the tax form instructions and software programs to implement this bill. The DOR's current level of resources should be sufficient to implement the program.

(Revised) *Indiana Economic Development Corporation:* The IEDC will incur additional expenses to establish the IMNJ tax credit program. The IEDC will be required to develop an application, process applications, certify community investments, monitor investment projects, and provide an annual report to the State Budget Committee. The IEDC will process all the fees paid by the applicants as defined within the bill. The IEDC's current level of resources should be sufficient to implement the program.

The bill also requires the IEDC to issue letter rulings to taxpayers regarding the INMJ credit. A letter ruling is a written interpretation of tax law issued to a private individual. The bill states the IEDC has 60 days to respond to a request, but the IEDC may decline for good cause. The letter ruling binds the DOR, the IEDC, and it's agents until the taxpayer claims all the taxpayer's INMJ credits. In addition, the letter ruling only applies to the requesting taxpayer. The IEDC's current level of resources should be sufficient to provide letter rulings.

(Revised) *Family and Social Services Administration (FSSA):* The bill establishes in statute the Paths to QUALITY^{tm} program. The program is to be a voluntary child care facility quality rating and improvement system implemented by the FSSA in partnership with the organizations specified in the bill. The bill requires the FSSA to adopt rules to administer the program. The FSSA should be able to comply with the provisions in the bill with their current level of staffing and resources because the program has been fully implemented since 2009.

Explanation of State Revenues: *Sales Tax Zapper Penalty*: If additional court cases occur and fines are collected, revenue to both the Common School Fund (from criminal fines) and the state General Fund (from court fees) would increase. The maximum fine for a Class C felony is $10,000. However, any additional revenues would likely be small.

(Revised) *Summary-IMNJ Tax Credit* The Indiana New Markets Job Tax Credit is designed to attract private investments in economically distressed neighborhoods. The total credit equals 39% of the Qualified Equity Investment (QEI) made by a qualified Community Development Entity (CDE) and is claimed over a seven-year period. Each year, the taxpayer applies the appropriate percentage to the QEI to determine the annual credit amount:

1. 0% for the first and second year
2. 7% for the third year
3. 8% for the fourth, fifth, sixth, and seventh year

The credit is effective for QEI made or acquired in CY 2013, CY 2014, or CY 2015. INMJ credits can be awarded for QEIs made in that year. The fiscal impact of credits awarded in CY 2013 will occur in FY 2016 due to the applicable percentage tiers. The estimated revenue loss in FY 2016 is approximately $4.27 M with the estimated revenue loss totaling $9.15 M in FY 2017. The usage of the credit is limited based on the QEI certified by the IEDC. The IEDC must limit the amount of QEI certified as to not exceed $10 M in tax credits per state fiscal year.

A portion of the revenue loss may be offset by an indeterminable amount of fee revenue received. All applicants must pay a nonrefundable application fee of $5,000, which is deposited in the state General Fund. Applicants also must pay a conditionally refundable $500,000 performance fee. If this fee is not refunded to the qualified CDE, it is deposited in the state General Fund as well.

(Revised) ***Background*** - Applicants are required to pay a $5,000 fee when applying to the IEDC. This fee is deposited in the state General Fund. The applicant is also required to pay a $500,000 conditionally refundable fee to the IEDC. The refundable fee is placed into the New Markets Performance Guarantee Fund. The $500,000 will be returned to the taxpayer upon meeting the investment conditions before the second credit allowance date. If the taxpayer fails to meet the conditions, the fee is transferred to the state General Fund.

The credit can be used to offset tax liabilities from the Individual Adjusted Gross Income Tax, Corporate Adjusted Gross Income Tax, Financial Institutions Tax, and Insurance Premiums Tax. Revenue collected from those taxes is deposited in the state General Fund. The credit is nonrefundable, but the taxpayer may carry forward unused credits to subsequent years. The credit may not be carried back or transferred. In addition, the total credits may not exceed $10 M per state fiscal year.

The Center for Business and Economic Research at Ball State University conducted a study on the effectiveness of the federal New Markets Tax Credit Program (NMTC) and how a state-level version of the NMTC affected overall levels of investment. The study found that states with their own version of a New Markets Tax Credit had higher levels of NMTC investments. They ran a simulation on the impact of Indiana implementing a 39% state version of the NMTC. The simulation estimated that an Indiana New Markets program would attract $433 M dollars in investments over a seven-year period. That is an average of $61 M QEI a year.

However, the model results were based on the federal NMTC. The INMJ credit has some slight differences. The federal program does not require fees to apply for the credit. The INMJ excludes child care providers with a Paths to QUALITY^{tm} rating of less than 4. In addition, the bill excludes businesses primarily engaged in home ownership services and those businesses who derive 15% or more of their annual revenue from the rental or sale of real estate.

Assuming Indiana attracts $61 M QEI per year, the first year the INMJ credits for those investments may be used to offset a tax liability would be FY 2016. This is due to the applicable credit percentage tiers. The INMJ credit amount is spread over a seven-year period. In addition, the bill requires the QEI to be made during CY 2013, CY 2014, or CY 2015.

The taxpayer may not use the INMJ credit for the first two years following the qualifying investment. Then, the credit equals 7% of the qualifying investment in year three and 8% of the qualifying investment in year four, five, six, and seven. So, the last year an INMJ tax credit could be claimed for a qualifying investment made in tax year 2013 would be tax year 2019, with the fiscal impact of that last year's credit occurring in FY 2020. The IEDC would have to certify a total of $125 M QEI to reach the $10 M per fiscal year credit limit. If $61 M QEI is authorized in CY 2013 and CY 2014 and $3 M in CY 2015 the maximum annual revenue loss of $10 M would occur beginning in FY 2019.

Explanation of Local Expenditures: *Sales Tax Zapper Penalty*: If more defendants are detained in county jails prior to their court hearings, local expenditures for jail operations may increase. However, any additional expenditures would likely be small.

Interest Rate: This provision would require that all interest collected by the county treasurer on property tax bills and interest paid to taxpayers on property tax refunds is calculated at the interest rate set by the DOR Commissioner. In addition, this provision requires that the appropriate year's interest rate applies for each year of the interest calculation.

This provision could increase or reduce interest payments to taxpayers, depending on whether the DOR interest rate is higher or lower than 4% for a given year. Property tax refunds reduce current year property tax collections for civil taxing units and school corporations.

Under current law, the interest rate used to compute interest payments to a taxpayer who receives a property tax refund because of a reduction in assessed value is 4% per year. The 2013 DOR interest rate is 3%. The last five years of DOR interest rates are as follows:

Year	Interest Rate
2009	7%
2010	4%
2011	9%
2012	4%
2013	3%

The interest rate is currently equal to the rate set by DOR if the taxes are refunded because:

(1) Taxes were paid more than once;
(2) The taxes were illegal; or
(3) There was a mathematical error in the computation of either the assessment or the taxes.

Interest paid by taxpayers for additional taxes billed because of assessments made or increased after the tax due date is currently charged at the DOR rate.

Explanation of Local Revenues: *Residential Circuit Breaker*: The bill defines common areas for purposes of the circuit breaker cap beginning with taxes payable in CY 2014. CY 2012 tax bills for apartments and other non-homestead residential property were examined to estimate the fiscal impact of this provision. The application of the 2% cap to the entire property would have reduced net taxes and increased revenue losses due to the circuit breaker in CY 2012 by a total of about $17.2 M. Apartment net taxes would be reduced by $8.3 M while other nonhomestead residential property tax would be reduced by about $8.9 M. The $17.2 M for CY 2012 would have to be refunded. Property tax refunds reduce current year property tax revenue for the taxing units that provide services to the property. The estimated annual revenue loss in future years is about the same.

The treatment of common areas as residential property for circuit breaker purposes also makes them eligible for residential property tax credits that counties may optionally provide from LOIT revenues. A fixed total amount of credits is spread among all eligible residential properties in the county. The additional eligible properties would cause a very slight decrease in residential credits for existing residential property.

[Under current law, residential property that is not a homestead is subject to the 2% circuit breaker cap. Nonhomestead residential property includes the dwelling, common areas, and land matching the building footprint. Beginning with taxes payable in CY 2014, this bill would define common areas to include roads, swimming pools, tennis courts, basketball courts, playgrounds, carports, garages, other parking areas, gazebos, decks, and patios, and all land used in connection with a building or structure. Most of these items currently qualify under the 3% circuit breaker cap but would qualify for the 2% cap under this bill.]

Abatements: Currently, designating bodies may use the statutory abatement schedules or they may use an alternative abatement schedule. In the alternative schedule, the percentage of deduction and the length of the abatement, not to exceed 10 years, is set by the designating body based on the following factors:

1. The total amount of the taxpayer's investment;
2. The number of new jobs created and the average wage as compared to minimum wage; and
3. The infrastructure requirements for the taxpayer's investment.

This bill would repeal the statutory schedule and would require designating bodies to establish an abatement schedule for each deduction allowed. Most deductions would be unaffected as the alternative schedules may now be used in most cases.

However, under current law, abatements in residentially distressed areas are limited to 5 years rather than ten years. Also, abatements for eligible vacant buildings are limited to 2 years. Under this provision, the designating body could authorize all abatements for up to 10 years. The terms of each abatement would be a local decision.

Sales Tax Zapper Penalty: If additional court actions occur and a guilty verdict is entered, local governments would receive revenue from court fees. However, the amounts would likely be small.

(Revised) *Homestead Deductions*: This provision could extend the standard deduction, supplemental standard deduction, and 1% circuit breaker cap to properties that initially don't qualify because construction of the dwelling was not completed by the assessment date. Additional deductions cause a property tax shift from the taxpayers receiving the deduction to all other taxpayers. Application of the 1% property tax cap could cause an increase in the amount of lost revenues due to the cap.

Under the bill, a taxpayer would receive the standard deduction on a newly constructed home if:

(1) The taxpayer interest is conveyed after the assessment date;

(2) Either the property was vacant or the construction on the dwelling was incomplete, on the assessment date;

(3) The taxpayer files the deduction application by December 31; and

(4) The taxpayer files a statement with the county auditor that lists other property that would otherwise receive the deduction and cancels the deduction on that property.

Under current law, homesteads receive a standard deduction worth 60% of AV up to $45,000. Homesteads also receive the supplemental standard deduction worth 35% on the first $600,000 of net AV after the standard deduction plus 25% of the net AV that exceeds $600,000. In addition, homestead property is subject to a 1% circuit breaker cap.

A homestead is defined as an individual's principal residence that the individual owns, is buying under contract, is entitled to occupy as a tenant-stockholder of a cooperative housing corporation, or one that is owned by certain trusts.

State Agencies Affected: Department of Correction.

Local Agencies Affected: Local assessors; County auditors; County treasurers; Local civil taxing units and school corporations; Trial courts, local law enforcement agencies.

Information Sources: Hicks, Michael J. and Dagney Faulk. "*The Effect of State-Level Add-On Legislation to Federal New Market Tax Credit Program.*" February 2012; Internal Revenue Service, "*New Markets Tax Credit.*" May 2010; Community Development Financial Institutions Fund, U.S. Department of the Treasury, http://www.cdfifund.gov/what_we_do/programs_id.asp?programID=5; LSA parcel-level property tax database.

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