

**LEGISLATIVE SERVICES AGENCY
OFFICE OF FISCAL AND MANAGEMENT ANALYSIS**

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FISCAL IMPACT STATEMENT

LS 6976
BILL NUMBER: SB 209

DATE PREPARED: Dec 28, 2000
BILL AMENDED:

SUBJECT: Repeal of Inheritance Tax.

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FUNDS AFFECTED: **GENERAL**
DEDICATED
FEDERAL

IMPACT: State & Local

Summary of Legislation: The bill provides that the Inheritance Tax does not apply to property interest transfers from the estate of a person who dies after June 30, 2001. The bill also repeals the Inheritance Tax effective July 1, 2003. The bill amends the Indiana Estate Tax formula and provides that the amended formula applies to the estate of a person who dies after June 30, 2001. The bill also makes conforming amendments.

Effective Date: July 1, 2001; July 1, 2003.

Explanation of State Expenditures: *Department of State Revenue:* Once the Inheritance Tax is repealed, there could be a savings to the state from a reduction in staff in the Inheritance Tax Section of the Department of State Revenue. The December 2, 2000, state manning table indicates that the Inheritance Tax Section employs 17 staff members with an annual salary cost of \$456,000. 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.

County Inheritance Tax Replacement: In addition to eliminating Inheritance Tax revenue to the state, the bill would eliminate the resident Inheritance Tax revenue retained by the counties. The revenue loss to counties is estimated to be approximately \$11.0 M statewide during FY 2003. As a result of the revenue loss, the bill would increase expenditures from the state General Fund relating to the Inheritance Tax replacement for counties. The maximum amount of county replacement for any year is \$7,452,000. With the repeal of the Inheritance Tax, this amount would continue to be paid to the counties. In addition, since the Inheritance Tax does not have to be paid until a maximum of 18 months after the decedent's death (within 12 months of the date of death to receive the 5% early payment discount), the impact that the bill may have on county replacement would be somewhat delayed.

Explanation of State Revenues: The bill is expected to reduce state revenue by an estimated \$127.5 M

beginning in FY 2003. The bill could also increase Estate Tax revenue by an estimated \$48.64 M in FY 2003. The net impact of the bill on state revenue is estimated to be a loss of approximately \$78.86 M in FY 2003. Further, the impact of state expenditures on county replacement increases the estimated loss to the state (net revenue loss plus county replacement expenditures) to approximately \$86.3 M in FY 2003. The estimated impact of the bill on Inheritance Tax and Estate Tax revenue and the net loss to the state including county replacement funding is presented below in Table 1.

TABLE 1

STATE IMPACT	FY 2003
Inheritance Tax Revenues	(\$127,500,000)
Estate Tax Revenues	\$48,637,283
Less: State Expenditures for County Replacement	(\$7,452,000)
Net Increase (Decrease)	(\$86,314,717)

Background on Inheritance Tax: The bill would eliminate the Inheritance Tax beginning with transfers from persons who die after June 30, 2001. Since the Inheritance Tax does not have to be paid until a maximum of 18 months after the decedent's death (within 12 months of the date of death to receive the 5% early payment discount), the full impact of eliminating the tax likely would not be experienced until FY 2003.

The estimated revenue loss is based on the Revenue Technical Committee's FY 2003 forecast for the Inheritance Tax equal to \$150 M. This total includes revenue from the Estate Tax estimated to be approximately 15% based on FY 2000 collections. This suggests that Inheritance Tax revenue is forecast at \$127.5 M. Thus, the revenue loss for FY 2003 is estimated to be \$127.5 M.

Background on Estate Tax: The reduction in Inheritance Tax liabilities for some taxpayers could potentially have an impact on Indiana Estate Tax revenues. Indiana Estate Tax is owed on the assets of an estate if (1) federal Estate Tax is owed on the estate and (2) the Indiana portion of the federal state death tax credit (against the federal Estate Tax) exceeds the total Inheritance Tax paid by transferees of the estate. Consequently, for some estates a reduction in the Inheritance Tax liability paid by transferees of the estate results in a compensating increase in the Estate Tax liability.

The estimated impact of the bill on Estate Tax revenues is based on an Office of Fiscal and Management Analysis (OFMA) database of Estate Tax returns relating to a decedent who died between July 1, 1997, and June 30, 2000. The database consists of 559 estates upon which Indiana Estate Tax was paid. It is assumed that the sample is representative of the universe of estates paying the Indiana Estate Tax. The 20% Inheritance Tax credit provided for in the bill led to a 43% increase in the Estate Tax liability of the sample. Based on the FY 2003 revenue forecast and FY 2000 collections, Estate Tax revenue is estimated to be \$22.5 M. Elimination of the Inheritance Tax led to a 216% increase in the Estate Tax liability of the sample. Thus, the revenue gain from the Estate Tax in FY 2003 is estimated to be \$48.64 M.

Explanation of Local Expenditures:

Explanation of Local Revenues: The repeal of the Inheritance Tax is estimated to result in a net revenue loss to counties of \$3.56 M beginning in FY 2003. The impact on the counties is presented below in Table

2.

Counties retain 8% of the Inheritance Tax collected on transfers made by Indiana residents. The estimated revenue loss statewide to counties beginning in FY 2003 is specified below in Table 2. It is important to note that a reduction in the amount of Inheritance Tax retained by counties due to the bill may be reimbursed by the state under the replacement provision established by P.L. 254-1997. Table 2 also specifies the amount of replacement funding the counties will receive beginning in FY 2003. The replacement provision was established when the Class A exemption was increased on July 1, 1997. The replacement provision guarantees that in each fiscal year each county receives an amount under the Inheritance Tax that is equal to the five-year annual average amount of Inheritance Tax revenue retained by that county from FY 1991 to FY 1997, excluding the highest and lowest year. A copy of a spreadsheet showing the amount of Inheritance Tax replacement guaranteed to each county under P.L. 254-1997 is available from the Office of Fiscal and Management Analysis.

TABLE 2	
Impact on Counties	FY 2003
Inheritance Tax Revenues	(\$11,008,696)
State Expenditures for County Replacement	\$7,452,000
Net Increase (Decrease)	(\$3,556,696)

State Agencies Affected: Department of State Revenue.

Local Agencies Affected: Counties.

Information Sources: State Revenue Forecast, December 19, 2000.
Bill Reynolds, Indiana Department of State Revenue, 232-2075.
OFMA Inheritance and Estate Tax Databases.
OFMA County Replacement Spreadsheet.