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**FISCAL IMPACT STATEMENT**

**LS 6486**

**BILL NUMBER:** HB 2008

**NOTE PREPARED:** Apr 7, 2003

**BILL AMENDED:** Apr 7, 2003

**SUBJECT:** Economic Development Matters.

**FIRST AUTHOR:** Rep Crawford

**FIRST SPONSOR:** Sen. Borst

**BILL STATUS:** CR Adopted - 2<sup>nd</sup> House

**FUNDS AFFECTED:**  GENERAL  
 DEDICATED  
 FEDERAL

**IMPACT:** State & Local

**Summary of Legislation:** (Amended) This bill includes the following provisions:

- (1) The bill changes the membership of the Indiana Economic Development Council.
- (2) The bill creates the Emerging Technology Grant Fund and Program.
- (3) The bill specifies the purposes for which the Rural Development Council may spend appropriations and creates an advisory board to make recommendations concerning those expenditures.
- (4) The bill authorizes the designation of tax allocation projects in distressed counties.
- (5) The bill creates a grant office within the Department of Commerce to work with federal agencies, state agencies, colleges and universities, and private sector entities to develop and receive research and development grants.
- (6) The bill establishes a property tax deduction for manufacturers who purchase depreciable personal property used to manufacture recycled components composed of at least 15% coal combustion waste generated in Indiana. It also establishes an income tax credit for manufacturers who manufacture recycled components consisting of at least 15% coal combustion waste generated in Indiana.
- (7) The bill provides that a person is not required to register as a retail merchant or to collect or remit the state sales or use tax in Indiana if the sole contact with Indiana is a contract with a call center in Indiana that provides telephone call services to the person.

(8) The bill exempts sales of certain energy-efficient appliances from the state Gross Retail Tax for sales occurring after June 30, 2003, and before January 1, 2008.

(9) The bill establishes a property tax deduction for 100% of the assessed value of aircraft owned or operated by certain air carriers or scheduled air taxi operators that have an Indiana corporate headquarters. It also provides that those aircraft are subject to the aircraft excise tax.

(10) The bill provides tax credits for the production of biodiesel and the production and retail sale of blended biodiesel. It also provides a tax credit for the production of ethanol in Indiana.

(11) The bill requires the Public Employees' Retirement Fund (PERF) and the Teachers' Retirement Fund (TRF) to apply for a grant from a private foundation or other entity to develop a fellowship program to assist PERF and TRF in increasing venture capital investment opportunities in Indiana technology and advanced manufacturing companies.

(12) The bill extends the expiration date for the Research Expense Tax Credit.

(13) The bill specifies that a pass through entity is eligible for the Venture Capital Investment Tax Credit for investments made in qualified Indiana businesses. The bill eliminates certain requirements that a business must meet in order to be certified as a qualified Indiana business. It also sets forth procedures for the Department of Commerce to certify that a taxpayer is entitled to a Venture Capital Investment Tax Credit. The bill provides that if a taxpayer carries over any credit amount to the succeeding year, the amount carried over does not count toward the \$10,000,000 in maximum allowable credits for the succeeding year.

(14) The bill authorizes the Indiana Port Commission to construct and finance: (1) maritime and nonmaritime port projects throughout Indiana for the transfer of goods and passengers between all modes of transportation; and (2) nonport projects to promote economic growth and development throughout Indiana. It also specifies the powers of the Commission with respect to these projects, including the conditions under which the Commission may issue bonds.

(15) The bill creates a Government Efficiency Commission.

(16) The bill makes appropriations for various purposes.

**Effective Date:** (Amended) January 1, 2003 (retroactive); Upon Passage; July 1, 2003; January 1, 2004.

**Summary of Net State Impact:** (Revised) The bill makes appropriations from the Build Indiana Fund in FY 2004 and FY 2005. The appropriations and the purposes of these appropriations are presented in the table below. Although the bill makes appropriations from the Build Indiana Fund during the 2003-2005 biennium, funds may not be available for these appropriations. If state and local capital projects receiving appropriations in the 2001-2003 Biennial Budget (P.L. 291-2001) are given priority when money is available in the Build Indiana Fund (BIF), sufficient revenue likely will not be available in BIF during FY 2004 and FY 2005 for the appropriations in the bill. Based on current estimates of BIF resources, revenue available for state and local projects is expected to total only \$13.8 M in both FY 2004 and FY 2005. Currently, however, there are \$242.5 M in appropriations for state and local capital projects under the 2001-2003 Biennial Budget that are suspended and have yet to be allotted money from BIF.

	<b>FY 2004</b>	<b>FY 2005</b>
<b>21<sup>st</sup> Century Research and Technology Fund</b>	\$5,000,000	\$20,000,000
<b>I-Light Fiber Optic System</b>	\$10,000,000	\$5,000,000
<b>Emerging Technology Grant Fund</b>	\$5,000,000	\$5,000,000
<b>Economic Development Partnership Fund</b>	\$5,000,000	\$5,000,000
<b>Value Added Research Fund</b>	\$500,000	\$500,000
<b>Indiana Rural Development Council</b>	\$1,000,000	\$1,000,000
<b>Government Efficiency Commission</b>	\$100,000	\$0
<b>PRF/TRF Venture Capital Fellowships</b>	\$200,000	\$200,000
<b>Corporate Tax Restructuring Publicity</b>	\$500,000	\$500,000
<b>Dept. of Commerce Grant Office</b>	\$50,000	\$50,000
<b>County Economic Dev. Office Grants</b>	\$2,300,000	\$0
<b>Public-Private Partnership for Econ. Dev. Mission</b>	\$125,000	\$125,000
<b>Total</b>	<b>\$29,775,000</b>	<b>\$37,375,000</b>

**Explanation of State Expenditures:** (Revised) *IEDC Board Membership and Authority:* The bill changes the membership of the Indiana Economic Development Council (IEDC) so that it is composed of 21 members, none of whom can be members of the General Assembly. The Governor and Lt. Governor each appoint three members; and the Speaker of the House of Representatives, President Pro Tempore of the Senate, House Minority Leader, and Senate Minority Leader each appoint two members. Also, the presidents of Indiana University, Purdue University, Indiana State University, Ball State University, Ivy Tech State College, Vincennes University, and the University of Southern Indiana each appoint one member. The bill provides that IEDC Board members are entitled to a salary per diem equal to the per diem for members of the General Assembly for attending meetings. In addition, Board members are to be reimbursed for actual and necessary expenses on the same basis as state employees. Under current law, the IEDC Board is composed of the Governor, the Lt. Governor, the chief operating officers of the IEDC, the Corporation for Indiana's International Future, and additional persons appointed by the Governor. The bill requires the Board to elect an executive director of the IEDC. The bill also allows the IEDC to employ bond counsel, other legal counsel, technical experts, and other officers, agents and employees.

*Emerging Technology Grant Fund:* The bill creates the Emerging Technology Grant Fund and Grant Program to be administered by the 21st Century Research and Technology Fund Board. The bill appropriates \$5,000,000 annually in FY 2004 and FY 2005 from the Build Indiana Fund for purposes of the Fund. The Fund is established to provide grants to match federal grants or other financial assistance for small technology-based businesses in an effort to accelerate the commercialization of emerging technologies. An eligible business must: (1) be independently owned and operated; (2) must have its principal office in Indiana; and (3) have either 100 or fewer employees or average annual gross receipts of \$10 M or less during the two calendar years preceding the year of application for the grant. (A manufacturing business must meet (1), (2), and the employment requirement in (3).) In addition to meeting these conditions, the business must

be engaged in life sciences, information technology, advanced manufacturing, or logistics. Money in the Fund at the end of the fiscal year does not revert to the General Fund.

The bill requires the 21st Century Research and Technology Fund Board to administer the Emerging Technology Grant Program. The bill specifies some criteria for awarding grants and requires the Board to establish guidelines for priority areas, matching levels, and maximum grant amounts.

*Rural Development Council:* The bill appropriates from the Build Indiana Fund \$1.0 M annually in FY 2004 and FY 2005 to the Rural Development Council to:

- (1) create, assess, and assist a pilot project to enhance the economic and community development in a rural area.
- (2) establish a local revolving loan fund for an industrial, a commercial, an agricultural, or a tourist venture.
- (3) provide a loan for an economic development project in a rural area.
- (4) provide technical assistance to a rural organization.
- (5) assist in the development and creation of a rural cooperative.
- (6) address rural workforce development challenges.
- (7) assist in addressing telecommunications needs in a rural area.
- (8) carry out the responsibilities of the rural development advisory board.

The bill prohibits the Council from spending the appropriations for these purposes unless the expenditure is recommended by the Rural Development Administration Advisory Board established by the bill. The Advisory Board consists of 16 members with four-year terms. The four legislative members of the Advisory Board are non-voting members. Each member who is not a state employee is entitled to the minimum salary per diem. Each member is entitled to reimbursement for traveling expenses and other expenses incurred in connection with the members' duties. Legislative members are entitled to legislative per diem, mileage, and travel allowance. Per diem and expenses of legislative members are to be paid from appropriations made to the Legislative Council or the Legislative Services Agency.

*Income/Sales Tax Allocation in Distressed Counties:* The bill establishes administrative responsibilities for several agencies. The additional administrative responsibilities established under the bill presumably could be absorbed by these agencies given their existing budgets and resources. The bill requires the Indiana Development Finance Authority (IDFA) to review and designate industrial development tax allocation areas in distressed counties. The State Budget Agency also must approve of the tax allocation areas. Under current statute, the Indiana Department of Commerce must provide administrative assistance to the IDFA. Currently, the IDFA has a staff of approximately eight.

The bill gives the Department of State Revenue (DOR) responsibility for determining base (sales and income tax) allocation amounts for purposes of tax allocations in industrial development project areas. These expenses presumably could be absorbed given the DOR's existing budget and resources. The Auditor of State is required to administer the industrial development project area funds established in connection with tax allocation areas designated by the IDFA. These expenses presumably could be absorbed given the Auditor's existing budget and resources. The bill also requires the Department of Workforce Development (DWD) to annually provide to the IDFA a list of the counties that meet distress criteria for purposes of designating tax allocation projects.

*IDOC Grant Office:* The bill creates a Grant Office in the Indiana Department of Commerce (IDOC) to be a clearinghouse of: (1) available research and development grant funding sources, and (2) certain Indiana

public and private entities that might benefit from federal and private research and development grants. These clearinghouse functions could potentially be performed electronically via an Internet website as has been done in other states (i.e., Georgia, Illinois, Maryland, and Wisconsin) and by higher education institutions. Such a website could be created and maintained by existing staff. The bill also *authorizes* the Grant office to assist entities seeking federal or private research and development funding in preparing grant applications and other documentation. The bill appropriates \$50,000 annually in FY 2004 and FY 2005 from the Build Indiana Fund for purposes of the Grant Office.

*Coal Combustion Products Reuse Tax Credit:* The Department of State Revenue (DOR) would incur some administrative expenses relating to the revision of tax forms, instructions, and computer programs to incorporate the tax credit. The Department also would have to monitor fiscal year credits claimed during a taxable year for purposes of the aggregate credit limit, and report certain information to the Center for Coal Technology Research. These expenses presumably could be absorbed given the DOR's existing budget and resources.

*Coal Combustion Products Reuse AV Deduction:* When new business personal property is added to the tax base, part of the property tax burden shifts from real property to business personal property, causing the state's expense for regular PTRC and Homestead Credits to be reduced. The property tax deduction allowed by this bill would delay part of the shift to the new business personal property for one year, which in turn would also delay part of the state expense reduction. However since this deduction may only be used in the first year of assessment and may not be allowed if the taxpayer is granted the income tax credit, the impact to the state's PTRC and Homestead credits may be negated. The bill provides that the deduction is applicable beginning with property taxes first due and payable in 2005.

The state pays Property Tax Replacement Credits (PTRC) in the amount of 60% of school general fund levies attributable to all property and 20% of the portion of all operating levies (including the remaining 40% of the school GF levy) that are attributable to real property and non-business personal property. Homestead Credits are paid by the state in the amount of 20% of the net property tax due for qualifying funds on owner-occupied residences.

PTRC and Homestead Credits are paid from the Property Tax Replacement Fund, which is annually supplemented by the state General Fund. Therefore, any change in PTRC or Homestead Credit payments would ultimately impact the state General Fund.

*Sales Tax Exemption on Qualified Energy-Efficient Appliances:* The bill would require the Department of State Revenue to develop rules associated with the establishing the Energy Star exemption. Any impact on the Department is expected to be absorbed using its existing staff and resources.

*Ethanol and Biodiesel Tax Credits:* The DOR would be required to develop forms and procedures related to these credits. Any impact is expected to be absorbed using its existing staff and resources.

*Indiana Recycling and Energy Development Board:* Taxpayers owning ethanol production facilities seeking the ethanol production tax credit offered in this bill are required to have the Board certify that the plant is eligible for the credit. The Board is expected to absorb any costs associated with certifying a facility using its existing staff and resources.

*PERF/TRF Venture Capital Fellowships:* The bill requires the PERF Board and the TRF Board to seek funding to develop a two-year fellowship program to work with the boards to enhance venture capital

investment opportunities in Indiana technology and advanced manufacturing companies. The bill requires the boards to seek funding from: (1) a private foundation; (2) the federal government; (3) an institution of higher education; or (4) any other entity. The bill appropriates \$200,000 annually in FY 2004 and FY 2005 from the Build Indiana Fund use by the boards for consulting services to supplement or provide matching funds for a grant from a private foundation for funding to develop a fellowship program to increase venture capital investment opportunities in Indiana technology and advanced manufacturing companies.

The Ewing Marion Kauffman Foundation of Kansas City, Missouri, has a new funding program launched to promote research into new business formation and entrepreneurial growth called The Emerging Scholars Grant program. The program is designed to accelerate research into entrepreneurial activity. The five Ph.D. student recipients of the Kauffman Emerging Scholars Initiative will each receive a maximum of \$15,000 to support academic research into entrepreneurship.

*Venture Capital Investment Tax Credit:* The Indiana Department of Commerce (IDOC) would incur additional administrative expenses relating to certification of qualified venture capital investment plans and monitoring credit awards relative to the annual credit maximum. These expenses presumably could be absorbed given the IDOC's existing budget and resources. The March 4, 2003, state staffing table indicates that the IDOC has 36 vacant full-time positions, including regional office positions.

*Port Commission:* The bill expands the Port Commission's authority beyond financing and building port projects on Lake Michigan, the Ohio River, and the Wabash River. In addition to its current powers, the bill authorizes the Port Commission to issue revenue bonds under its current law issuing authority to finance projects involving (1) to (3) below.

(1) Ports on other water bodies in Indiana.

(2) Nonmaritime port and traffic exchange points throughout Indiana for the transfer of goods and passengers between all modes of transportation.

(3) Any other project located in Indiana other than at a port, that the Commission finds will enhance, foster, aid, provide, or promote: (a) economic development; (b) public-private partnerships; and (c) other industrial, commercial, business, transportation purposes.

Under current statute, Port Commission revenue bonds have a maximum maturity of 50 years. Also under current statute, Port Commission revenue bonds do not constitute a debt, or a pledge of the faith and credit, of the state or political subdivisions of the state. In addition, current statute requires that revenue bonds of the Port Commission be secured with revenues derived by the Commission from fees, tolls, rentals, and other charges for: (1) the use of Commission ports, projects, terminal facilities, and lands; or (2) services rendered by the Commission. Current law authorizes the Port Commission to fix its fees, tolls, rentals, and other charges to provide revenue sufficient to pay its administrative, operation, and maintenance costs and the principal and interest on revenue bond issuances. As a result of the bill, the Port Commission would incur additional administrative expenses relating to the expansion of project financing authority. Additional staffing that may be necessitated by this expansion is unknown at this time. The Port Commission currently has 11 employees staffing its Indianapolis office, with 23 port employees located in Mt. Vernon, Jeffersonville, and Portage.

*Government Efficiency Commission:* The bill creates an 11-member commission consisting of a representative of the State Board of Accounts; a designee of the Lt. Governor; a designee of the Secretary

of State; four appointees of the Speaker of the House; and four appointees of the President Pro Tempore of the Senate. The Commission is established to develop specific recommendations on the best practices to streamline, improve, and consolidate procedures for state government dealings among departments, with individuals, with businesses, and with other levels of government. Each member who is not a state employee is entitled to the minimum salary per diem. Each member is entitled to reimbursement for traveling expenses and other expenses incurred in connection with the members' duties. Legislative members are entitled to legislative per diem, mileage, and travel allowance. The bill appropriates \$100,000 in FY 2004 for the operation and purposes of the Commission. The bill requires the following individuals to provide staff for the Commission: the Chief Information Officer of the state, a deputy budget director designated by the State Budget Director, a deputy commissioner of the Department of Administrative Services designated by the Commissioner of the Department, and a deputy director of the State Personnel Department designated by the Director of the Department.

*Indiana Economic Development Partnership Fund:* This Fund exists under current statute to provide grants for certain economic development initiatives. The bill shifts administration of grant application and approval procedures to the Indiana Department of Commerce under agreement with the State Budget Agency (SBA). (The SBA currently fulfills these functions.) The bill also authorizes the SBA to contract with Purdue University for staff support in providing grants relating to the expansion of the Purdue Technical Assistance Program and the Purdue Rural/Community Economic Development Regional Outreach Program. The bill appropriates \$5,000,000 annually in FY 2004 and FY 2005 from the Build Indiana Fund for purposes of the Fund.

*Tax Restructuring Publicity:* The bill appropriates \$1.0 M during the 2003-2005 biennium from the Build Indiana Fund to the Indiana Department of Commerce to publicize the corporate tax restructuring in Indiana to businesses and industries in other states.

*County Economic Development Office Grants:* The bill appropriates \$2.3 M in FY 2004 from the Build Indiana Fund to the Indiana Department of Commerce to provide grants totaling \$25,000 to each county upon written request to be used by the county economic development office. A *county economic development office* is an entity established by a county or jointly by a county and one or more cities or towns in the county with the primary purpose of: (1) promotion of industrial or business development; (2) the retention or expansion of Indiana businesses; or (3) the development of entrepreneurial activities in Indiana. This does not include an economic development commission, redevelopment commission, regional planning commission, or urban enterprise association established under state law.

*Public-Private Partnership for Economic Development Mission:* The bill appropriates \$250,000 during the 2003-2005 biennium from the Build Indiana Fund to the Governor for use to create and operate a nonprofit corporation to establish a public-private partnership to assist in guiding the economic development mission of the state.

*I-Light Fiber Optic System:* The bill appropriates \$10.0 M in FY 2004 and \$5.0 M in FY 2005 from the Build Indiana Fund for the purpose of improving high-speed data access and communications capability statewide by linking fiber optic infrastructure to 11 areas around the state (I-Light Fiber Optic System).

**Explanation of State Revenues:** (Revised) *Income/Sales Tax Allocations in Distressed Counties:* The bill provides for the allocation of incremental state Sales, Use, and Adjusted Gross Income (AGI) tax revenue to pay for industrial development projects designated by the Indiana Development Finance Authority (IDFA). These tax allocation projects are limited to counties determined under the bill to be "distressed areas."

Currently, there are six counties that would qualify under the bill (Blackford, Fayette, Greene, Lawrence, Orange, and Starke), and two other counties could potentially qualify in the near future (Pulaski and White). The amount of incremental tax revenue that could potentially be allocated to pay the costs of tax allocation projects statewide is indeterminable. The amount of incremental tax revenue diverted to tax allocation projects presumably does not represent a revenue loss to the state to the extent that the incremental revenue is attributable to the industrial development project or subsequent economic activity in project facilities. However, the state does incur a revenue loss to the extent that the diverted revenues are attributable to underlying growth in tax revenue. Sales and Use Tax collections increased from FY 1998 to FY 2002 by an annual average of 3.75%. During the same period, individual AGI Tax collections increased about 0.8% annually. (This includes the one-year decline in FY 2002 of about 6.3%.) From FY 1998 to FY 2001, however, individual AGI Tax collections increased by an average of 3.26% annually. These provisions of the bill are effective July 1, 2003. Thus, depending upon how quickly the IDFA begins the tax allocation project designation process, the bill could potentially impact state revenue beginning in FY 2004, but more likely in FY 2005.

*Coal Combustion Products Reuse Tax Credit:* The bill would reduce state Adjusted Gross Income (AGI) Tax liabilities of individual and corporate taxpayers that obtain and use coal combustion products from a facility located in Indiana for the manufacturing of recycled components. This tax credit is expected to reduce AGI Tax revenue by \$2.0 M annually. The revenue loss could potentially begin the second half of FY 2004 (due to changes in estimated tax payments) or FY 2005.

The bill establishes a nonrefundable individual and corporate AGI Tax credit for manufacturers that obtain and use coal combustion products for the manufacturing of recycled components. The bill defines *coal combustion products* as by products resulting from the combustion of coal in a facility located in Indiana, including a fluidized bed boiler. Coal combustion products include boiler slag, bottom ash, fly ash, and scrubber sludge. Tangible personal property is a *recycled component* if coal combustion products constitute at least 15% by weight of the property. The credit is equal to \$2 per ton of increased acquisitions during the taxable year of coal combustion products obtained and used by a manufacturer. Businesses that already use coal combustion products would have to show at least a 10% increase in use over the highest of the preceding three years to claim the credit. Under the bill, a taxpayer is not entitled to a refund, carryback, or carryforward of excess credits. In addition, the bill limits the number of years that a taxpayer may claim the credit to 10 consecutive years. The bill limits the aggregate credits claimed during a taxable year to \$2.0 M. Thus, total credits may be claimed each year for usage totaling up to 1.0 M tons.

The table below reports the approximate 1999 total production of coal combustion products and amount and percent reused for seven utilities in Indiana (NiSource, Cinergy, AEP, Vectren, Hoosier Energy, IKEC, and IPL). This indicates that annual unused tonnage could potentially total about 4.8 M tons. However, the amount of creditable reuse in a taxable year could potentially exceed this total assuming: (1) some annual growth in production of coal combustion products; (2) year-to-year variation in reuse by individual taxpayers; and (3) turnover in those entities reusing coal combustion products.



<b>1999 Coal Combustion Products Totals</b>			
<b>Product</b>	<b>Tons Produced</b>	<b>Tons Reused</b>	<b>Percent Reused</b>
Flyash	3,287,072	1,130,152	34%
FGD Materials	3,779,295	1,839,141	49%
Bottom Ash	1,162,642	497,420	43%
<b>Total</b>	<b>8,229,009</b>	<b>3,466,713</b>	<b>42%</b>

*Call Center Exemption:* The exemption for call centers is not expected to have a direct impact on the state's current Sales Tax revenues, nor will it remove the responsibility of Indiana consumers to pay the Use Tax on items purchased from out-of-state firms. However, the bill could cause the state to forgo potential Sales Tax remittances by the affected contracted call centers and out-of-state firms.

This bill will allow out-of-state firms that do not have an otherwise significant presence in Indiana to establish a contractual relationship with a call center located in Indiana and remain excluded from the state's Sales Tax collection requirements. The proposal will not exempt firms that would otherwise have a significant presence in the state from collecting and remitting the Sales Tax. Indiana residents who purchase goods from out-of-state firms are responsible for paying Indiana's Use Tax.

*Sales Tax Exemption on Qualified Energy-Efficient Appliances:* This bill temporarily exempts the sale of clothes washers, refrigerators, dishwashers, and room air conditioners that meet or exceed the Energy Star efficiency standards developed by the U.S. Environmental Protection Agency (EPA) and the U.S. Department of Energy (DOE) from the state Sales Tax. The exemption is limited to sales that occur from June 30, 2003, to January 1, 2008. It is estimated that over the life of the exemption period the impact on state revenues will be as follows:

FY 2004	(5.1 M)
FY 2005	(5.0 M)
FY 2006	(5.5 M)
FY 2007	(6.3 M)
FY 2008	(3.3 M)
<b>Total</b>	<b>(\$ 25.3 M)</b>

The estimates shown above are based on the average price of each type of qualified Energy Star appliance, the estimated market share of the different types of Energy Star appliances, and the estimated total number of units of each type of appliance sold in Indiana. The analysis also assumed that the bill's effective reduction in the price of qualified appliances would impact the number purchased by approximately 2% each year. This increase is in addition to the estimated growth in the market share of Energy Star appliances as a result of changes in federal standards and in manufacturing efficiencies. If more energy-efficient appliances are purchased as a result of this bill, the state may see further reductions in Sales Tax income generated from the sale of electricity, natural gas, and water. Estimates suggest that if the bill encourages the purchase of 2% more Energy Star-rated appliances in Indiana each year, Sales Tax revenue for the sale of utilities could be reduced by as much as \$57,000 per year.

*Blended Biodiesel Tax Credits:* The impact of the tax credits for the production and sale of biodiesel and blended biodiesel is unknown; however, it is presumed to be relatively small. The tax credits related to the production and sale of biodiesel are not capped. The bill provides a credit of \$1.00 for each gallon of biodiesel manufactured in Indiana after January 1, 2004. Biodiesel is defined as a renewable biodegradable, mono alkyl ester combustible liquid fuel derived from agricultural plant oils or animal fats. Biodiesel is not currently produced in the state. If, however, enough pure biodiesel were produced to generate enough B2 blended biodiesel (petroleum diesel blended with 2% biodiesel) to replace 1% of the diesel purchased in Indiana for transportation, the credit would equal approximately \$200,000. Producing enough biodiesel to generate enough B2 blended biodiesel to replace 10% of the petroleum diesel used for highway transportation would result in a credit equal to \$2.0 M. It is not known how much biodiesel would be produced as a result of this credit. The National Biodiesel Board reports that there are 15 active legal plants in the United States and that approximately 10 M to 12 M gallons of biodiesel were consumed during CY 2002.

The bill also provides a credit of \$0.02 for each gallon of blended biodiesel (petroleum diesel blended with at least 2% biodiesel) produced in Indiana using biodiesel produced in Indiana. The impact of the credit is also unknown. However, again using the example shown above, if 1% of the petroleum diesel used in Indiana for transportation were replaced with Indiana-produced B2 biodiesel, the credit would equal about \$200,000. Replacing 10% of the petroleum diesel used for transportation would result in a credit equal to about \$2.0 M per year.

The biodiesel production and blending credits above would be reduced by any federal credit or subsidy that the taxpayer receives for producing or blending biodiesel.

The bill also establishes a \$0.01 credit for each gallon of blended biodiesel (petroleum diesel blended with at least 2% biodiesel) sold by Indiana retailers. If 1% of the petroleum diesel used in Indiana for transportation were replaced with Indiana-produced B2 biodiesel, the credit would equal about \$100,000 per year.

*Ethanol Production Tax Credit:* The bill caps the total amount of ethanol production tax credits allowed to all taxpayers in all taxable years at \$10.0 M. The bill provides a tax credit equal to \$0.125 per gallon of ethanol produced at qualified facilities. To be eligible to receive the credit, the ethanol must be produced at a facility that has the capacity to produce at least 40 M gallons of ethanol each year and be constructed after December 31, 2003, or an existing facility that increases production capacity by 40 M gallons a year after December 31, 2003. The facility would be required to be certified as eligible to receive the credit by the Indiana Recycling and Energy Development Board. The bill limits each taxpayer to a total credit amount of \$5.0 M. The total amount of ethanol production tax credits allowed to all taxpayers in all taxable years is capped at \$10.0 M.

The producer and retailer tax credits are not refundable, but may be carried forward to subsequent years. Taxpayers are not entitled to a carryback with either tax credit. If a taxpayer is a pass through entity and does not have a tax liability, the credit could be taken by shareholders, partners, or members of the pass through entity in proportion to their distributive income from the pass through entity. Since the tax credits are effective beginning in tax year 2004, the fiscal impact could potentially begin in the second half of FY 2004 (due to sales tax credits and changes in estimated quarterly income tax payments). Revenue from the AGI Tax on corporations, the Insurance Premiums Tax, and the Financial Institutions Tax is distributed to the state General Fund. Eighty-six percent of the revenue from the AGI Tax on individuals is deposited in the state General Fund, and 14% of this revenue is deposited in the Property Tax Replacement Fund. Since the

tax credits are effective beginning in tax year 2004, the fiscal impact would begin in FY 2005. Sales Tax revenue is deposited in the Property Tax Replacement Fund (50%), the state General Fund (49.192%), the Public Mass Transportation Fund (0.635%), the Commuter Rail Service Fund (0.14%), and the Industrial Rail Service Loan Fund (0.033%).

It should be noted that reductions in state revenue as a result of the biodiesel and ethanol credits may be offset with tax receipts associated with increases in employment, capital expenditures, and other taxable activity that may not have occurred absent the incentives provided in the amendment.

*Research Expense Credit:* This bill extends the expiration date of the Research Expense Credit to December 31, 2010. It is currently set to expire December 31, 2004. It is estimated that these changes will result in an additional revenue loss beginning in FY 2005 through FY 2011.

Over the past few years, the current Research Expense Credit has ranged from \$9.2 M in FY 1996 to \$24.2 M in FY 1999. However P.L. 192-2002ss increased the credit to 10% and eliminated the apportionment formula. Consequently the cost of the base credit was estimated to increase by an additional \$47.9 M in FY 2004 and \$51.5 M in FY 2005 (for a full 12 months or \$24.8 M for 6 months due to the expiration of the credit in 2004). The total annual cost of the current credit is estimated to be \$72.1 M in FY 2004 and \$75.7 M in FY 2005. If this credit were to expire December 31, 2004, the revenue base could potentially increase by approximately \$37.85 M in FY 2005 (six months liability) and \$79 M in FY 2006. However, without this credit available, taxpayers' investment in research activities could significantly change and affect their base income tax liabilities. Research Expense Tax Credits affect revenue collections deposited in the General Fund.

It is difficult to estimate the exact impact of continuing this tax credit since it is dependent on both the amount of research expenses individual taxpayers make during the year and their total tax liability. With additional incentives created for research and development activity based in the state of Indiana, the revenue loss from this credit could increase by an indeterminable amount. The credit provides \$100,000 for each \$1 M in new research expenses. Increased expenditures on research activities could also generate additional Adjusted Gross Income and Sales Tax revenue if these expenses are used to hire additional employees or purchase related equipment.

*Venture Capital Investment Tax Credit:* The bill changes the calculation of the annual aggregate credit limit of \$10 M. The bill provides that the \$10 M annual limit on total credits allowed applies only to the new credits certified for venture capital provided during that taxable year. Thus, carryover credits claimed in a taxable year are not counted toward the \$10 M annual maximum. This change could increase the annual total credits claimed above the existing statutory limit of \$10 M per year in tax years 2005 to 2008. This could potentially reduce revenue by an amount greater than \$10 M in FY 2006 to FY 2009. This would be contingent on the amount of carryover credits and new credits that taxpayers are able to claim in a tax year. However the total amount of the credits allowed over the lifetime of the credit will not change.

The bill also makes changes to the criteria for certifying a business as a qualified Indiana business for venture capital investment that may be claimed by the investor under the Venture Capital Investment Tax Credit. These changes could potentially increase the number of businesses in which creditable venture capital investment may be made.

*Port Commission:* Under current statute, ports and other property of the Port Commission, interest on Commission revenue bonds, proceeds from the sale of the bonds, and receipt of the interest and proceeds is

exempt from taxation in Indiana, except for the Financial Institutions Tax and the Inheritance Tax. The bill extends this tax-exempt status to nonmaritime port facilities and nonport projects of the Commission that are authorized by the bill. Thus, the bill could result in the exemption of additional investment income from taxation to the extent that taxpayers substitute investment in Port Commission revenue bonds for investments in taxable instruments.

### **Explanation of Local Expenditures:**

**Explanation of Local Revenues:** (Revised) *Coal Combustion Products Reuse Tax Incentives:* The bill provides an AV deduction for depreciable personal property that a manufacturer purchases and uses to manufacture recycled components containing at least 15% coal combustion products by weight. (See *Explanation of State Revenues* for discussion of coal combustion products and usage.) A manufacturer would be entitled to the AV deduction only in the first year that the depreciable personal property is subject to assessment. The bill provides that the deduction is applicable beginning with property taxes first due and payable in 2005.

The allowable deduction is equal to 15% of the assessed value of the personal property. The bill prohibits a taxpayer from obtaining the Coal Combustion Product Tax Credit (see above under *Explanation of State Revenues*) during the taxable year that the taxpayer obtains this AV deduction. Data is unavailable relating to potential future investment in personal property used to manufacture products containing coal combustion products, or the typical value of such property. Additional deductions reduce the assessed value tax base. This causes a shift of the property tax burden from the taxpayers receiving the deductions to all taxpayers in the form of an increased tax rate. Total local revenues, except for cumulative funds, would remain unchanged. The revenue for cumulative funds would be reduced by the product of the fund rate multiplied by the deduction amount applicable to that fund.

*Airline Property Tax:* Effective with property taxes paid in 2004, this bill would provide a 100% property tax deduction for (1) passenger aircraft with a seating capacity of 90 passengers or less and (2) cargo aircraft that are owned by an air carrier or scheduled air taxi operator. To qualify for the deduction, the owner must have its corporate headquarters in Indiana or be a subsidiary of another corporation with its headquarters in Indiana.

The two airline taxpayers in Indiana that would have been impacted by the provision have reincorporated in Indiana as of February 26, 2003. Under current law, as Indiana corporations, these taxpayers will not be liable for property tax on aircraft beginning with taxes paid in 2004 and will instead pay aircraft excise tax.

If any airlines qualify for this exemption in the future, the additional deductions would reduce the assessed value tax base causing a shift of the property tax burden from the taxpayers receiving the exemptions to all taxpayers in the form of an increased tax rate.

*Port Commission:* Under current statute, ports and other property of the Port Commission are exempt from property taxation in Indiana. The bill extends this tax-exempt status to nonmaritime port facilities and nonport projects of the Commission that are authorized by the bill. In addition, the bill extends a current property tax exemption for leaseholds in Port Commission land. Under current law, a lessee's leasehold estate in land that is part of a port is exempt from property tax. Under the bill, a lessee's leasehold estate in land that is part of a nonmaritime port facility authorized by the bill is also exempt from property taxation. The bill could potentially affect property tax revenue to local units given that it substantially expands the types of projects that the Port Commission may finance and build. This fiscal impact would arise due to the

tax-exempt status of Port Commission property and the property tax exemption relating to land provided to lessees of Port Commission facilities.

**State Agencies Affected:** Indiana Department of Commerce; Indiana Development Finance Authority; State Budget Agency; 21<sup>st</sup> Century Research and Technology Fund Board; State Treasurer; Lt. Governor; Governor; Department of Workforce Development; Commissioner of Agriculture; Department of State Revenue; Port Commission; Legislative Services Agency; Department of Local Government Finance; Auditor of State.

**Local Agencies Affected:** Assessors; Auditors.

**Information Sources:** Department of State Revenue; Department of Local Government Finance; Local Government Database; Department of Workforce Development. R. James Meiers, Indianapolis Power and Light, (317) 261-5185; Association of Home Appliance Manufacturers; U.S. Bureau of Labor Statistics, *Consumer Expenditure Survey*; Bill McNary, D and R International, 301-588-9387; U.S. EPA and U.S. Department of Energy, [www.energystar.gov](http://www.energystar.gov); Federal Highway Administration, 2001 Highway Statistics; National Biodiesel Board.

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