LEGISLATIVE SERVICES AGENCY
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FISCAL IMPACT STATEMENT

LS 6531 | **NOTE PREPARED:** Jan 6, 2004
BILL NUMBER: SB 466 | **BILL AMENDED:**

SUBJECT: Elimination of Inheritance Tax.

FIRST AUTHOR: Sen. Ford | **BILL STATUS:** As Introduced
FIRST SPONSOR:

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

Summary of Legislation: This bill provides that the state Inheritance Tax does not apply to property interest transfers from the estate of a person who dies after June 30, 2004. It also amends the Indiana Estate Tax formula with respect to the estate of a person who dies after June 30, 2004 and makes conforming amendments.

Effective Date: July 1, 2004.

Explanation of State Expenditures: Under the bill, the state will no longer receive revenue from the Inheritance Tax beginning in FY 2006 but will experience a compensating increase in Estate Tax revenue in FY 2006. In addition, the bill is expected to increase state General Fund expenditures on county Inheritance Tax replacement. The net state impact of the bill is summarized in the table below.

Fiscal Year	Inheritance Tax Revenues	Estate Tax Revenues	State Expenditures for County Replacement	Net Increase (Decrease)
FY 2006	($101.5 M)	$ 3.9 M	($7.4 M)	($105.0 M)
FY 2007 and after	(101.5 M)	0.0	(7.4 M)	(108.9 M)

Department of State Revenue: Once the Inheritance Tax is repealed, there could be a savings to the state from a reduction in staff of the Inheritance Tax Section of the Department of State Revenue. The December 3, 2003, State Staffing Report indicates that the Inheritance Department has 15 full-time employees with an annual salary of $464,528. Since staff will be needed to process returns on estates that owe tax before the law is repealed, a specific savings due to staff reductions could not be estimated.

County Inheritance Tax Replacement: Elimination of the Inheritance Tax would increase expenditures for the state General Fund for county Inheritance Tax replacement by approximately $7.4 M annually beginning in FY 2006. This is the maximum amount guaranteed to counties under the replacement procedure. (See *Explanation of Local Revenues*, below, for explanations of county revenue loss and replacement procedures.)

Explanation of State Revenues: The bill is expected to eliminate approximately $101.5 M annually in Inheritance Tax Revenues beginning in FY 2006. The reduction in Inheritance Tax liability is expected to increase Indiana Estate Tax revenue by $3.9 M in FY 2006. The Estate Tax offset is expected to decline to zero in FY 2007 as the phase out of the federal state death tax credit (begun in 2002) is completed. The net revenue loss from the bill is estimated to total $105.0 M in FY 2006 and $108.9 M per year beginning in 2007.

Background on Inheritance Tax: The bill would eliminate the Inheritance Tax applicable to transfers made by persons who die on or after July 1, 2004. Since the Inheritance Tax does not have to be paid until a maximum of 12 months after the decedent's death (within nine months to receive the 5 percent early payment discount), the full impact of the bill would not occur until FY 2006.

The estimated impact of the elimination of the Inheritance Tax is based on the Revenue Technical Committee's FY 2004 forecast (updated April 10, 2003). The forecast estimates FY 2004 combined Inheritance and Estate Tax revenues to be $120 M. Based on a four-year average (2000-2003), 84.6 percent of the forecast revenue is estimated to be attributable to the Inheritance Tax. From these estimates, the Inheritance Tax will yield about $101.5 M, and the Estate Tax will yield about $18.5 M in FY 2004. These revenue estimates are used as the base for the fiscal impact analysis.

Background on Estate Tax: The elimination of the Inheritance Tax would affect Estate Tax revenues. Under current statute, 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 state death tax credit for federal Estate Tax purposes exceeds the total Inheritance Tax paid by transferees of the estate, so the Indiana Estate Tax is equal to the difference between the death tax credit and Indiana Inheritance Tax. Under the bill, the Indiana Estate Tax would still be limited to estates paying federal Estate Tax and will equal the death tax credit. This could substantially increase Indiana Estate Tax Revenues for some estates. The federal Estate Tax is set to expire in 2005, as will the Indiana Estate Tax which is linked to the federal tax. As such, the revenue impact of the bill will affect the Indiana revenues only for FY 2006.

The estimated impact of the bill on Estate Tax revenues is based on OFMA's Estate Tax database and the Revenue Technical Committee's FY 2004 Estate Tax forecast (updated April 10, 2003) of $18.5 M. The Estate Tax database consists of 559 estates of decedents who died between July 1, 1997, and June 30, 2000, and that paid Indiana Estate Tax. The elimination of the Inheritance Tax is estimated to increase Estate Tax Revenue by approximately $3.9 M in FY 2006.

Explanation of Local Expenditures:

Explanation of Local Revenues: The repeal of the Inheritance Tax will result in a net annual revenue loss to counties totaling $1.4 M. The table below shows the decrease in county revenues resulting from the bill.

	Annual Impact Beginning in FY 2006
County Inheritance Tax Revenues (Decrease)	($8.8 M)
State Expenditures for County Replacement	7.4 M
Net Increase (Decrease)	(1.4 M)

Counties retain 8 percent of the Inheritance Tax collected on transfers made by Indiana residents. About 99.3 percent of Inheritance Tax revenue is attributable to the resident Inheritance Tax. Based on the FY 2004 forecast of state Inheritance Tax Revenue totaling $101.5 M, annual county Inheritance Tax revenue will be approximately $8.8 M beginning in FY 2004. Counties are guaranteed a statutorily determined amount as determined by the replacement provision established by P.L. 254-1997. The replacement provision was established to replace county Inheritance Tax revenue lost when the Class A exemption was increased on July 1, 1997. The replacement provision guarantees that each county receives Inheritance Tax revenue equal to the five-year annual average amount of Inheritance Tax received by that county from FY 1991 to FY 1997 excluding the highest and lowest years. The Inheritance Tax replacement that the state guarantees counties totals $7.4 M per year. Approximately, $1.4 M of county Inheritance Tax revenue will not be replaced, which will be a net revenue loss to counties.

A copy of the 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.

State Agencies Affected: Department of State Revenues

Local Agencies Affected: Counties

Information Sources: State Revenue Forecast (April 10, 2003), OFMA Inheritance and Estate Tax databases.

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