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**FISCAL IMPACT STATEMENT**

**LS 6676**

**BILL NUMBER:** HB 1327

**NOTE PREPARED:** Mar 23, 2006

**BILL AMENDED:** Mar 14, 2006

**SUBJECT:** Taxation and Government Finance.

**FIRST AUTHOR:** Rep. Espich

**FIRST SPONSOR:** Sen. Kenley

**BILL STATUS:** Enrolled

**FUNDS AFFECTED:**  GENERAL  
 DEDICATED  
 FEDERAL

**IMPACT:** State & Local

**Summary of Legislation:** *Validation of Bonds:* The bill changes the date for validation of all outstanding bonds issued or lease agreements executed by various governmental entities from March 15, 2000, to March 15, 2006.

*Sales and Use Tax Deduction Assignability:* The bill prohibits the assignment of Sales Tax remittance deductions to nonaffiliated companies.

*Internal Revenue Code (IRC) Reference Update:* The bill provides that for taxable years beginning after December 31, 2005, references in Indiana law to the Internal Revenue Code and related regulations refer to the law and regulations in effect on January 1, 2006.

*Dependent Child Deduction:* The bill specifies that the category of children for which an additional \$1,500 state income tax deduction may be claimed is to be determined under an Internal Revenue Code definition as it was in effect on January 1, 2004.

*Jackson County CAGIT:* The bill extends to June 30, 2011, the time during which Jackson County may impose an additional County Adjusted Gross Income Tax rate of 0.1% for the operation of a jail and juvenile detention center.

*Scott County COIT:* The bill permits an additional County Option Income Tax rate in Scott County to construct and maintain criminal justice facilities.

***Nashville Food & Beverage Tax:*** The bill changes the termination date for the Nashville Food and Beverage Tax from January 1, 2007, to January 1, 2012.

***Martinsville Food & Beverage Tax:*** The bill extends the deadline for initiating projects under the Martinsville Food and Beverage Tax from December 31, 2010, to December 31, 2015.

***School Pension Bonds:*** The bill allows a school corporation to petition the DLGF requesting approval to incur bond indebtedness to implement solutions to contractual retirement or severance liability.

**Effective Date:** Upon Passage; January 1, 2005 (retroactive); January 1, 2006 (retroactive); March 15, 2006 (retroactive); July 1, 2006; July 1, 2007.

**Explanation of State Expenditures: Validation of Bonds:** Under existing law, all bonds, notes, evidences of indebtedness, leases, or other written obligations issued by or in the name of any state agency, county, township, city, incorporated town, school corporation, state educational institution, state-supported institution of higher learning, political subdivision, joint agency created under IC 8-1-2.2 (which involves municipal electric utility programs), leasing body, or any other political, municipal, public or quasi-public corporation or in the name of any special assessment or taxing district; or in the name of any commission, authority, or authorized body of any such entity; and any pledge, dedication or designation of revenues, conveyance, or mortgage securing these bonds, notes, evidences of indebtedness, leases, or other written obligations are hereby legalized and declared valid if these bonds, notes, evidences of indebtedness, leases, or other written obligations have been executed before March 15, 2000.

The bill provides that in addition to the above-listed debt instruments, swap agreements and other agreements are legalized. Additionally, the bill includes "boards" with respect to entities to which the provisions apply. The bill further extends the deadline before which the debt instrument must have been executed, from March 15, 2000, to March 15, 2006.

Essentially, these provisions legalize the above-mentioned products. Without the provision, if, for example, a bond was issued without providing the appropriate notice, the bond could be invalidated. The above provisions make the issuer or the entities involved not liable. For example, IC4-4-11-17 provides that the Indiana Finance Authority must hold a public hearing on the proposed financing agreement for an industrial development project after giving notice by publication in one newspaper of general circulation in the city, town, or county where the industrial development project is to be located at least ten days in advance of this public hearing. Under the bill, if the notice was given only six days in advance of the public hearing, the Authority could not be held liable and the bond would not be invalidated.

***State Tax Changes:*** The Department of State Revenue (DOR) will incur additional expenses to revise tax forms, instructions, and computer programs to reflect the changes contained in this bill. The DOR's current level of resources should be sufficient to implement these changes.

***Scott County COIT:*** The DOR and the State Budget Agency (SBA) will be required to adjust Scott County's COIT certified distribution for the year following a tax rate increase authorized under the bill. The resource levels of the DOR and the SBA should be sufficient to carry out these tasks.

Any overpayments of the distribution due to local option tax rate increases will be covered by the state General Fund until adjusted in the subsequent year distributions.

**Explanation of State Revenues: Sales and Use Tax Deduction Assignability:** This bill provides that for transactions occurring after June 30, 2007, a retail merchant may *NOT* assign the Sales and Use Tax deductions allowed under IC 6-2.5-6-9 to any individual or group that is not part of the same "affiliated group" as the taxpayer assigning the deduction. Affiliated group is defined in the bill as either of the following.

- (1) An affiliated group within the meaning provided in Section 1504 of the Internal Revenue Code, except that the ownership percentage in Section 1504(a)(2) of the IRC shall be determined using 50% test rather than 80% test, or a relationship described in Section 267(b)(11) of the IRC.
- (2) Two or more partnerships, including LLCs and LLPs, that have the same degree of mutual ownership as an affiliated group described in (1).

IC 6-2.5-6-9 allows a retail merchant deductions for transactions:

- (1) where the merchant did not collect Sales or Use Tax from the purchaser;
- (2) where the merchant previously paid Sales or Use Tax on the transaction; and
- (3) which were written off as uncollectible debt for federal tax purposes under section 166 of the Internal Revenue Code.

**IRC Reference Update:** The bill updates the reference to the Internal Revenue Code to incorporate all the federal changes made up to January 1, 2006. The current reference to the IRC pertains to all IRC provisions amended and in effect on January 1, 2005. The update would include changes affecting tax years 2005 and after as a result of the following federal acts:

- (1) The Energy Tax Incentives Act of 2005 (P.L. 109-58);
- (2) The Katrina Emergency Tax Relief Act of 2005 (P.L. 109-73);
- (3) The Gulf Opportunity Zone Act of 2005 (P.L. 109-135).

The Energy Tax Incentives Act includes provisions relating to: (1) depreciation and expensing of natural gas distribution property, electricity transmission and distribution property, and certain refinery investments; (2) amortization of certain air pollution control facilities installed by electric generating companies; and (3) deduction for construction of energy-efficient commercial buildings.

The Katrina Emergency Tax Relief Act and the Gulf Opportunity Zone Act include provisions: (1) increasing corporate charitable contribution limits; (2) excluding from gross income charitable mileage reimbursements for volunteers; and (3) expanding the deduction for corporate contributions of food inventory to noncorporate entities, and extending the deduction to donations of books to public schools. A summary of the estimated revenue impact of these federal acts is outlined in the table below.

<b>Provisions (Revenue Impact in \$M)</b>	<b>FY 2006</b>	<b>FY 2007</b>	<b>FY 2008</b>
<b>Energy Tax Incentives Act</b>			
(1) Depreciation and expensing provisions.	(0.13)	(0.44)	(1.17)
(2) Amortization provisions.	(0.05)	(0.14)	(0.29)
(3) Deduction for energy-efficient commercial buildings.	(0.17)	(0.36)	(0.20)
(4) Other provisions.	(0.44)	(0.32)	(0.21)
<b>Subtotal</b>	<b>(0.79)</b>	<b>(1.26)</b>	<b>(1.87)</b>
<b>Katrina Emergency Tax Relief Act/Gulf Opportunity Zone Act</b>			
Charitable contribution provisions.	(0.49)	(0.15)	0.0
<b>Total Impact on State Revenue</b>	<b>(1.28)</b>	<b>(1.41)</b>	<b>(1.87)</b>

Revenue from the corporate AGI Tax is distributed to the state General Fund. The revenue from the individual AGI Tax is deposited in the state General Fund (86%) and the Property Tax Replacement Fund (14%).

**Explanation of Local Expenditures: Scott County COIT:** Scott County could use additional revenue generated by a rate increase in COIT to finance, construct, acquire, improve, renovate, equip, maintain, or operate their county jail. The county treasurer must establish a county jail revenue fund for the receipt of the additional revenue.

**Explanation of Local Revenues: IRC Reference Update:** The IRC update could potentially affect taxable income of individual taxpayers. However, the impact on counties imposing local option income taxes (CAGIT, COIT, and/or CEDIT) is likely to be minimal.

**Jackson County CAGIT:** The bill allows Jackson County the option to continue the imposition of CAGIT at a 1.1% rate for jail construction until July 1, 2011. Unless the county were to reduce the rate before the proposed expiration date, the impact to Jackson County revenues should be neutral.

*Background:* Jackson County's CAGIT CY 2006 certified distribution was \$7.3 M. The additional 0.1% rate has been effective since July 1, 1998. It is estimated that from CY 1999 to CY 2006, the county has averaged about \$685,000 in revenue per year at the 1.1% rate.

**Scott County COIT:** The bill allows the Scott County Council to increase the county's COIT rate by no more than 0.25% to fund jail improvement capital projects if the Council adopts an ordinance finding and determining that the additional COIT revenue is needed.

If an ordinance to increase the rate were adopted by the Council before June 1, 2006, or before April 1 of a subsequent year, the additional rate would be effective on July 1 in the year of adoption. If the ordinance were adopted after May 31, 2006, or after March 31, of a subsequent year, the rate would be effective July 1 in the

year following the year of adoption.

In either adoption scenario, Scott County would begin to receive revenue from the tax in the immediately following year. Therefore, if Scott County were to adopt the additional COIT rate in CY 2006, the county would begin to receive revenue from the rate increase in January 2007.

If a 0.25% rate increase were effective on July 1, 2006, the additional rate is estimated to generate approximately \$0.82 M in CY 2007, \$0.85 M in CY 2008, and \$0.87 M in CY 2009.

All revenue generated by an additional tax rate would be set aside for the jail before the certified distribution is divided between the civil taxing units in the county.

*Background:* Under the bill, Scott County is authorized to maintain a combined COIT and County Economic Development Income Tax (CEDIT) rate not exceeding 1.25% (with exception for any additional CEDIT rate adopted for homesteads.) Under current law, with a few exceptions, the maximum combined rate of COIT and CEDIT is 1.00%.

Scott County received a certified COIT distribution of \$3.2 M in CY 2006 at a 1.00% rate. The county also received a certified CEDIT distribution of \$0.48 M in CY 2006 at a 0.16% rate.

***Nashville Food & Beverage Tax:*** The bill allows a five-year extension from the current expiration date on the collection of Nashville's Food and Beverage Tax. For example, if the tax were imposed for an additional five years, with average annual revenues of \$125,000 per year, Nashville could receive an additional \$0.6 M over the proposed five-year extension.

*Background:* From FY 1996 to FY 2005, Nashville averaged \$125,000 annually from the tax. The average annual percent change over that time period was 2.3%. The tax was established by P.L. 111-1987. The revenue is used to construct and maintain public parking and restroom facilities.

***Martinsville Food & Beverage Tax:*** The bill extends the deadline for initiating projects under the Martinsville Food and Beverage Tax from December 31, 2010, to December 31, 2015. This provision should not affect revenue collection. The tax is currently imposed at a rate of 1%.

***School Pension Bonds:*** The bill provides that a school corporation that issued bonds to cover retirement or severance liability under a prior statute (which was repealed on December 31, 2004) may issue bonds one additional time for that purpose if the first bond issue was approved by the DLGF before April 14, 2003. (Current law permits a second bond issue only if the first bonds were actually issued before April 14, 2003.) The bill provides that the additional bonds must be issued before January 31, 2007.

An additional bond would be based on existing unfunded contractual liability for retirement or severance payments as of June 30, 2001. The school must reduce the transportation fund, school bus replacement fund, capital projects fund, or art association and historical society funds in an amount equal to the property tax levy needed to retire the pension or severance bonds. The pension bonds would be subject to the petition and remonstrance process. The bill would probably have minor impact on pension bonding of schools. To qualify, a school would have had to have the bonding approved but not issued the bond by the April 14, 2003, deadline.

*Background:* About 241 pension bonds worth over \$1.2 B have been approved by the Department of

Local Government Finance.

**State Agencies Affected:** Department of State Revenue; Department of Local Government Finance.

**Local Agencies Affected:** Counties with local option income taxes.

**Information Sources:** Tom Conley, Department of State Revenue, (317) 232-2107; Bob Lain, State Budget Agency, (317) 232-3471; U.S. Congress, Joint Committee on Taxation, <http://www.house.gov/jct/tableofcnts.html>; *Indiana Handbook of Taxes, Revenues, and Appropriations*.

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