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FISCAL IMPACT STATEMENT

LS 6830 **NOTE PREPARED:** Jan 7, 2006
BILL NUMBER: SB 351 **BILL AMENDED:**

SUBJECT: Indiana Displaced Worker Tax Credit.

FIRST AUTHOR: Sen. Lanane **BILL STATUS:** As Introduced
FIRST SPONSOR:

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

Summary of Legislation: The bill provides that a taxpayer that hires an Indiana displaced worker is eligible to claim a credit against state tax liability if the taxpayer: (1) pays the worker at least the federal minimum wage; and (2) is not an affiliate, parent, or subsidiary of or successor in interest to the worker's previous employer. It provides that the credit is equal to 10% of the annual compensation due to the worker. It also provides that if the taxpayer does not retain the worker for at least three years, the taxpayer must pay the amount of the credit to the state.

Effective Date: January 1, 2007.

Explanation of State Expenditures: The Department of State Revenue (DOR) will incur additional administrative expenses related to changing tax forms, instructions, and computer programs to accommodate the new tax credit. Under clawback provisions of the bill, the DOR also would have to monitor job tenure of displaced workers for whom credits have been claimed, and seek repayment of credit amounts by taxpayers who do not retain such workers for at least 3 years. The DOR's current level of resources should be sufficient to implement these administrative tasks.

Explanation of State Revenues: *Summary:* The bill would reduce state Adjusted Gross Income (AGI) Tax, Insurance Premiums Tax, and Financial Institutions Tax liabilities of individual and corporate taxpayers, including pass through entities, that employ qualified displaced workers in Indiana. The revenue loss due to this bill could potentially range from $39 M to $56 M annually based on historic displacement and re-employment patterns. The annual impact could potentially be lower to the extent that taxpayers have insufficient tax liabilities to utilize all credits to which they are entitled. The fiscal impact could begin in FY

2007 if taxpayers adjust their quarterly estimated payments.

Background: The bill establishes a nonrefundable tax credit to corporate and non-corporate businesses (including pass through entities) that employ displaced workers. The tax credit is equal to 10% of the first-year cost of wages and benefits paid to a displaced worker, and may be taken against the taxpayer's AGI Tax, Insurance Premiums Tax, or Financial Institutions Tax liability. In order to qualify for the tax credit, the business must employ a worker who had been employed in one job in Indiana for at least 3 years and who lost that job due to economic factors affecting the previous employer. The tax credit may not be claimed for workers previously terminated and then rehired by the business. In addition, the value of the wages and benefits paid to the displaced worker must equal at least 75% of the value of the wages and benefits paid in the displaced worker's previous employment. The bill also requires that the displaced worker be employed by the taxpayer for at least 3 years. If not, the credit is forfeited and must be repaid to the DOR. The penalty would not be enforced if the taxpayer released the displaced worker for cause within the 3-year period.

The tax credit is non-refundable, and unused credit amounts may not be carried back. However, a taxpayer may carry forward any unused credit amount for 5 successive taxable years. For pass through entities, the credit may be claimed by shareholders, partners, or members in proportion to their distributive income from the pass through entity.

Revenue from the AGI Tax on corporations, the Financial Institutions Tax, and the Insurance Premiums 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 the revenue is deposited in the Property Tax Replacement Fund. Since the tax credit is effective beginning in tax year 2007, the fiscal impact could potentially begin in FY 2007 if taxpayers adjust their quarterly payments.

The pool of displaced workers in Indiana could potentially total about 22,000 to 25,000 annually. This is based on the long-run average displacement rates (1991-1992 to 1999-2000) of workers with job tenure of three or more years estimated by the U.S. Bureau of Labor Statistics (BLS). The most recent BLS estimates also suggest that about 77% of displaced workers are re-employed within one year, with the median time unemployed equal to about 5.5 weeks. This suggests that 17,000 to 19,000 of the annual displaced workers are re-employed within a year. BLS estimates also suggest (based on 1991-1992 to 1999-2000 data) that about 65% to 75% of the displaced workers who are re-employed have earnings at the new job at least equal to 80% of their earnings in the prior job. Thus, employers could potentially hire 12,000 to 13,000 displaced workers annually that would qualify the employer for the tax credit. Current average annual compensation (pay and benefits) in Indiana is about $43,000. Assuming a displaced worker earned about the average at his or her prior job and the worker is re-employed at a compensation 75% to 100% of the prior compensation level (rates required by the bill), the cost of the tax credit for the employee would range from $3,225 to $4,300. The aggregate cost assumes that re-employed displaced workers would be retained in the new job for at least three years. Current estimates by the BLS indicate that the median job tenure in the U.S. is about four years.

Explanation of Local Expenditures:

Explanation of Local Revenues:

State Agencies Affected: Department of State Revenue.

Local Agencies Affected:

Information Sources: U.S. Bureau of Labor Statistics (BLS), *Employee Tenure Summary, September 2004.* BLS, *Displaced Workers Summary, July 2004.* BLS Distribution of Employed Wage and Salary Workers by Tenure, January 2004. BLS, *Worker Displacement in 1999-2000, Monthly Labor Review, June 2004.* BLS, *Covered Establishments, Employment, and Wages by State, 2005*. U.S. Bureau of Economic Analysis, *Compensation of Employees by Industry - Indiana, 2004*.

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