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**FISCAL IMPACT STATEMENT**

**LS 7696**

**BILL NUMBER: SB 500**

**NOTE PREPARED: Feb 20, 2007**

**BILL AMENDED: Feb 19, 2007**

**SUBJECT:** Tax Procedure and Administration Changes.

**FIRST AUTHOR:** Sen. Kenley

**FIRST SPONSOR:** Rep. Kuzman

**BILL STATUS:** As Passed Senate

**FUNDS AFFECTED:**  **GENERAL**  
 **DEDICATED**  
 **FEDERAL**

**IMPACT:** State

**Summary of Legislation:** (Amended) *Sales Tax Exemption Restrictions:* This bill restricts a Sales Tax exemption available under current law for an electric utility that purchases distribution equipment or transmission equipment. The bill also restricts a Sales Tax exemption available under current law for a hotel or a restaurant that purchases electricity, water, gas, or steam. The bill restricts a Sales Tax exemption available under current law for an aircraft lessor that purchases an aircraft for rental or leasing.

*Sales Tax Collection Allowance:* This bill provides for a graduated Sales and Use Tax collection allowance for a retail merchant.

*Electronic Returns and Funds Transfer Requirements:* This bill specifies conditions under which a professional tax return preparer must file client returns electronically. The bill decreases various periodic tax liability thresholds at which taxpayers are required to make tax payments by electronic fund transfer from \$10,000 to \$5,000. The bill provides that a tax payment made by electronic fund transfer is considered made on the date the taxpayer issues the payment order for the electronic fund transfer.

*Interest on Tax Refunds & Excess Payments:* The bill provides for the accrual of interest at the rate of 6% per annum on Inheritance Tax refunds that are not processed within 90 days by the Department of State Revenue (DOR). The bill specifies that the rate of interest paid by the DOR on excess tax payments must be the same as the rate of interest paid by a taxpayer for failing to pay the full amount of tax by the due date for a tax return. The bill also makes technical corrections.

*Cigarette Tax Stamp Discount:* The bill also increases the cigarette stamp discount to distributors from 1.2% to 2.523%.

*Refund Hearings:* The bill provides that when a taxpayer claiming a refund requests a hearing on the claim, the DOR must hold the requested hearing.

*Out-of-state Merchant Registration:* The bill also repeals a provision of the Sales Tax statute that requires certain out-of-state merchants making sales to customers in Indiana to register as retail merchants and remit Sales and Use Tax.

*NFL Sales Tax Exemption:* The bill provides a state Sales Tax exemption for transactions involving tangible personal property or services acquired by the National Football League or a professional football team to facilitate the league's holding of or the team's participation in a qualified football championship event. The bill also provides that an entity may claim the exemption only if, before acquiring the property or service, the entity applies for and receives from the department of state revenue a state gross retail tax exemption certificate.

*Tax Credit Repayments for Non-Qualified 529 Plan Withdrawals:* The bill provides that an account owner of a college choice 529 education savings plan must repay a portion of a tax credit if any non-qualified withdrawal is made from the plan. The bill also includes as non-qualified withdrawals any withdrawals made from an account that is terminated within 12 months after the account is opened, rollovers to another qualified tuition program under Section 529 of the Internal Revenue Code that is not a college choice 529 education savings plan account, and other withdrawals that do not meet the requirements of a qualified withdrawal.

*Aircraft Tax Exemptions:* The bill provides a limited Use Tax exemption for an aircraft that is titled or registered in another state or country and is temporarily brought to Indiana to be repaired, refurbished, remanufactured, or subjected to a prepurchase evaluation. The bill expands the limited Sales Tax exemption under current law for a transaction involving an aircraft to include transactions in which the aircraft that is purchased by a nonresident remains in Indiana for up to 30 days after the aircraft is repaired, refurbished, or remanufactured. The bill expands the exemption from the aircraft registration requirements under the aircraft license excise tax statute for a nonresident who bases an aircraft with a dealer while the aircraft is being repaired, remodeled, or refurbished to include aircraft that are based with a person that has been issued a repair station certificate by the Federal Aviation Administration.

*Public Transportation Exemption Verification:* The bill provides that a retail merchant may verify that the sale of property used or consumed in providing public transportation is exempt from sales tax by obtaining certain information from the purchaser. This bill allows a retail merchant that sold property to a person that used or consumed the property in providing public transportation to verify that the sale was exempt from sales tax by using the information contained in form ST-135 for the transaction.

*Penalty for Corporate Tax Underpayment:* The bill provides that the penalty for underpayment of estimated Corporate Income Tax is assessed only on the lesser of: (1) the difference between the actual amount paid by the corporation and 20% of the corporation's final tax liability for the taxable year; or (2) the difference between the actual amount paid by the corporation and 25% of the final tax liability for the corporation's previous taxable year. (Under current law, the penalty is assessed on the difference between the actual amount paid by a corporation on its estimated return and 25% of the corporation's final adjusted gross income tax liability for the taxable year.) The bill also provides that these changes apply to taxable years beginning after December 15, 2007.

**Effective Date:** (Amended) Upon Passage; January 1, 2007 (retroactive); July 1, 2007; January 1, 2008.

**Explanation of State Expenditures:** (Revised) *Summary of Expenditures:* It is estimated that this bill will result in overall administrative cost savings for the Department of State Revenue (DOR). All of these provisions will cause the DOR to amend forms, rules and procedures related to administration of the corporate and individual Adjusted Gross Income (AGI) taxes, the Sales Tax, the Inheritance Tax, the Financial Institutions Tax, the Motor Fuel Taxes, and the Cigarette Tax. Although, it is estimated that these increased costs will be totally offset by the administrative costs savings resulting from provisions in the bill.

The provisions of the bill estimated to result in administrative cost savings are as follows:

*Electronic Returns and Funds Transfer Requirements:* The bill lowers the threshold amount of tax liability that is required before the DOR may require payment by electronic funds transfer from \$10,000 to \$5,000. It is estimated that the incremental costs of receiving payments electronically is lower than receiving payment by other means. The exact amount of savings is indeterminable.

The bill also provides that if a professional tax preparer files more than 100 individual AGI Tax returns in a calendar year, then in the immediately following calendar year the preparer must file their returns electronically.

*Interest on Tax Refunds & Excess Payments:* This bill provides for the accrual of interest, from the date the refund is filed, at the rate of 6% per annum on Inheritance Tax refunds that are not processed within 90 days by the DOR. Under current law, the same rate of interest accrues, but from the date the tax was paid. It is estimated that this will result in a savings to the DOR. The savings will ultimately be determined by the difference in the amount of interest that would have been paid from the date the tax was paid versus the date the claim refund was filed. Any savings could be increased or offset by the provision in the bill specifying that the rate of interest paid by the DOR on excess tax payments must be the same as the rate of interest paid by a taxpayer for failing to pay the full amount of tax by the due date for a tax return. To the extent that the rate required by current statute for a rate of interest on excess payments differed from the rate of interest on taxpayer delinquencies there could be either a savings or increase in state expenditures. The impact of this provision is indeterminable.

*DOR Employee Incentives:* It is estimated that the DOR could realize a cost savings from the provision of the bill allowing them to establish production quotas for agents based on the number of cases closed. The amount of savings will ultimately be determined by the possible increase in productivity as a result of these incentives and quotas being implemented by the DOR.

The following provisions could result in an increase in administrative costs to the DOR.

*Refund Hearings:* The bill provides that when a taxpayer claiming a refund requests a hearing on the claim, the Department of State Revenue must hold the requested hearing. Under current law, the DOR may, but does not have to hold a hearing on a refund claim.

*Aircraft Tax Exemptions & NFL Sales Tax Exemption:* The DOR will have to amend Sales and Use Tax forms, and Aircraft License Excise Tax forms, as well as update computer software. The DOR could also be required to issue more Sales and Use Tax exemption certificates for certain entities. It is estimated that these provisions of the bill can be implemented within the existing level of resources available to the DOR.

*Tax Credit Repayments for Non-Qualified 529 Plan Withdrawals:* The DOR will incur additional expenses to revise tax forms, instructions, and computer programs, and to administer tax credit reduction and repayment programs under the bill. The bill would require the DOR to utilize information provided by the Education Savings Authority to collect repayments of tax credits claimed by a taxpayer for contributions to the taxpayer's Indiana College Choice 529 Investment Plan account if the taxpayer makes non-qualified withdrawals from that account. The Department's current level of resources should be sufficient to implement these changes. The February 19, 2007, state vacant position report indicates the DOR has 248 vacant full-time positions.

The impact of the following provisions on the administrative costs of the DOR are indeterminable.

*Sales Tax Exemption Restrictions:* This bill restricts a Sales Tax exemption available under current law for an electric utility that purchases distribution equipment or transmission equipment. The bill restricts a Sales Tax exemption available under current law for a hotel or a restaurant that purchases electricity, water, gas, or steam. This bill also restricts a Sales Tax exemption available under current law for an aircraft lessor that purchases an aircraft for rental or leasing.

Restricting these exemptions and specifying what these exemptions do and do not apply to could result in a savings to the DOR to the extent that fewer administrative actions are filed contesting DOR interpretation on the issues more clearly specified in this bill. Although, by adding specific restrictions to these exemptions could lead to more administrative hearings on whether the restrictions apply to certain taxpayers or certain situations. Any possible increase in cost could be offset by the increase in Sales Tax collections that could result from these provisions (see *Explanation of State Revenues*).

*Out-of-state Merchant Registration:* The bill also repeals a provision of the Sales Tax statute that requires certain out-of-state merchants making sales to customers in Indiana to register as retail merchants and remit Sales and Use tax. This provision could result in a cost savings for the DOR, by requiring the DOR to register fewer merchants. Although, it must be noted that any possible decrease in costs could be offset by the decrease in Sales Tax collections that could result from these provisions (see *Explanation of State Revenues*).

*Indiana Education Savings Authority:* The bill requires the Executive Director of the Authority to annually submit to the DOR a copy of all information returns or statements issued to taxpayers with respect to withdrawals or distributions made from an Indiana College Choice 529 Investment Plan account for the taxable year; or account closings for the taxable year.

**Explanation of State Revenues:** (Revised) *Revenue Summary:* The total impact of this legislation on state revenues is indeterminable. It is estimated that the provisions of the this bill will result in an overall increase in revenue from tax collections of *at least approximately \$10.7 M each year.*

This increase is based on the impact of the change in the Sales Tax collection allowance, offset by the increase in the discount on cigarette tax stamps. This table illustrates the impact of each provision and the overall sum of those impacts.

<b>Provision</b>	<b>Annual Impact</b>
<i>Sales Tax Collection Allowance Changes</i>	\$15.3 M
<i>Cigarette Tax Stamp Discount Increase</i>	(\$4.6 M)
<b>TOTAL</b>	<b>\$10.7 M</b>

*Aircraft Tax Exemptions:* These provisions of the bill could result in an indeterminable impact in Sales and Use Tax and Aircraft License Excise Tax (ALET). The bill provides for a new Use Tax exemption, and expands the Sales Tax exemption, for aircraft purchased by nonresidents. The bill also expands the exemption for nonresidents from registering an aircraft for the purposes of imposing the ALET. Any potential decrease in Sales or Use Tax revenue could be offset by a potential increase in Adjusted Gross Income Tax if this exemption provides an incentive for more repair work to be conducted in Indiana.

*Use Tax:* The bill provides that Use Tax may not be imposed on the exercise of any right or power over an aircraft if that aircraft is:

- (1) titled, registered, or based in another state or country;
- (2) delivered to Indiana by or for a nonresident owner or purchaser;
- (3) delivered to Indiana for the sole purpose of repair, refurbishment, remanufacture, or prepurchase evaluation (as defined in the bill); and
- (4) transported out of Indiana after completion of any work listed in item (3).

*Sales Tax:* The bill also amends the Sales Tax exemption for an aircraft purchased by a nonresident. Under current statute an aircraft is exempt from Sales Tax if:

- (1) purchased by a nonresident;
- (2) transported out of Indiana within 30 days of delivery; and
- (3) will be titled or registered for use in another state or country and not titled or registered in Indiana.

The bill moves the exemption to a new code cite, and adds certain provisions to the exemption requirements. The bill adds the ability for a nonresident purchaser to receive the exemption for an aircraft if it is transported out of Indiana within 30 days after completion of a repair, refurbishment, or remanufacture of the aircraft. The bill also adds that an exemption may be granted if the aircraft will be based in another state or country (in the case of a state or country that does not require an aircraft to be titled or registered.)

*Aircraft License Excise Tax:* The bill adds repair station (as defined in the bill) to the list of places a nonresident may base an aircraft for repair, refurbishment, or remodeling in Indiana for more than 60 days without registering the aircraft for the purposes of imposition of the ALET. Currently, an aircraft may only be exempt from this registration if the aircraft is based for repair, refurbishment, or remodeling in Indiana with a dealer. Please note that a nonresident only needs to complete the ALET registration if the aircraft will be based in Indiana for more than 60 days.

ALET revenues are distributed on a quarterly basis to the county where the aircraft is usually located when it is not being operated. However, in Allen County, the funds go to the Ft. Wayne Airport Authority quarterly.

*NFL Sales Tax Exemption:* This provision of the bill could cause an indeterminable impact on Sales Tax collections. The amount of the impact will be determined by:

- (1) the amount of Sales Tax not collected from transactions involving these entities; and
- (2) the possible increase in taxable sales resulting from a Super Bowl being held in Indiana.

Any impact will only be realized if a Super Bowl is held in Indiana.

The bill provides a Sales Tax exemption for transactions involving tangible personal property or services acquired by the National Football League or a professional football team to facilitate the league's holding of or the team's participation in a qualified football championship event. The bill also provides that an entity may claim this exemption only if, before acquiring the property or service, the entity applies for and receives from the DOR a state Gross Retail Tax exemption certificate.

*Sales Tax Collection Allowance:* The bill provides for a graduated Sales and Use Tax collection allowance for a retail merchant. The current rate is 0.83%, and the new rates are based on gross receipts of the merchants as follows:

<b>Annual Gross Receipts</b>	<b>Rate</b>	<b>Number of Taxpayers</b>	<b>Allowance Total under Current Rate (in millions)</b>	<b>Allowance Total under New Rate (in millions)</b>	<b>Impact on Sales Tax Collections (in millions)</b>
Less than \$60,000	0.83%	162,652	\$5.1	\$5.1	\$0
Greater than \$60,000 but less than \$600,000	0.60%	6,283	\$8.2	\$5.9	\$2.3
Greater than or equal to \$600,000	0.30%	913	\$20.4	\$7.4	\$13.0
	<b>TOTAL</b>	<b>169,848</b>	<b>\$33.7</b>	<b>\$18.4</b>	<b>\$15.3</b>

Please note that this estimate represents a simulation of the change in the collection allowances based on 2005 Sales Tax return data provided by the DOR. The actual impact on revenue collections will be dependent on sales tax transactions beginning July 1, 2007.

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 Fund (0.033%).

*Cigarette Tax Stamp Discount:* The bill increases the cigarette stamp discount to distributors from 1.2% to 2.523%. The increase in this discount will decrease Cigarette Tax collections by approximately \$4.6 M in FY 2008 and \$4.7 M in FY 2009. This estimate is based on data from the December 14, 2006, *State Revenue Forecast*.

*Sales Tax Exemption Restrictions:* To the extent that restricting these exemptions leads to less exemptions being awarded, there will be an indeterminable increase in Sales tax collections.

*Public Transportation Exemption Verification:* This provision of the bill is expected to have a minimal fiscal

impact on Sales and Use Tax collections. This bill provides that a retail merchant may verify an exempt sale of tangible personal property used or consumed in providing public transportation by obtaining certain information from the purchaser. The bill also provides that if a retail merchant previously sold tangible personal property to a person under this exemption for property consumed in providing public transportation and provides proof as previously contained in DOR form ST-135, the retail merchant may request a refund or satisfaction of outstanding liability from the DOR.

The impact of these changes will ultimately be determined by the actions of the DOR, retail merchants, and purchasers. These provisions do not change the number of exempt purchases that could occur, but rather, any impact will only be to the extent that these provisions allow purchasers to more easily obtain the exemption.

*Out-of-state Merchant Registration:* To the extent that repealing these registration and remittance requirements leads to fewer out-of-state merchants remitting Sales Tax, state revenues will decrease. Although, the impact of this provision is indeterminable. It must be noted that many out-of-state merchants now register to remit Sales Tax to various states under the Streamlined Sales Tax Agreement (SSTA).

*Tax Credit Repayments for Non-Qualified 529 Plan Withdrawals:* The bill provides that the owner of an Indiana College Choice 529 Investment Plan account who claimed tax credits during the taxable year or a prior taxable year for contributions to the account, must repay the tax credits if the account owner makes any non-qualified withdrawal from the account. The bill requires the repayment to be made in the taxable year in which the non-qualified withdrawal is made.

The bill defines a “qualified withdrawal” as a withdrawal or distribution from an Indiana College Choice 529 Investment Plan account that is made:

- (1) to pay for qualified higher education expenses, except when the savings plan is terminated within 12 months after the account is opened;
- (2) as a result of the death or disability of an account beneficiary;
- (3) because an account beneficiary received a scholarship that paid for the qualified higher education expenses, with the qualified withdrawal equal to or less than the scholarship amount; and
- (4) by an Indiana College Choice 529 Investment Plan as a result of a transfer of funds by a plan from one third-party custodian to another.

The bill specifies that a qualified withdrawal does not include a rollover distribution or transfer of assets from an Indiana College Choice 529 Investment Plan to any other qualified tuition program under Section 529 of the Internal Revenue Code that is not an Indiana College Choice 529 Investment Plan.

*Penalty for Corporate Tax Underpayment:* This provision of the bill could result in an indeterminable decrease in penalties collected for underpayment of estimated Corporate Adjusted Gross Income (AGI) Tax payments. The amount of the decrease is indeterminable, and will ultimately depend upon the specifics of any underpayment by a corporation in a particular taxable year. The bill provides that these changes apply to taxable years beginning after December 15, 2007; therefore, any impact could begin in the second half of FY 2008, but more likely would begin in FY 2009 due to the possible delay in the assessment of a penalty and reconciliation payment by a delinquent taxpayer.

The bill provides that the penalty for underpayment of estimated Corporate AGI Tax is assessed only on the lesser of: (1) the difference between the actual amount paid by the corporation and 20% of the corporation's final tax liability for the taxable year; or (2) the difference between the actual amount paid by the corporation

and 25% of the final tax liability for the corporation's previous taxable year. (Under current law, the penalty is assessed on the difference between the actual amount paid by a corporation on its estimated return and 25% of the corporation's final adjusted gross income tax liability for the taxable year.)

**Explanation of Local Expenditures:**

**Explanation of Local Revenues:** *Background Information on the Aircraft License Excise Tax:* In FY 2006, there was approximately \$595,000 in ALET collections. The weight, class, and age of the aircraft determine taxes owed. Revenues are distributed on a quarterly basis to the county where the aircraft is usually located when it is not being operated. However, in Allen County, the funds go to the Ft. Wayne Airport Authority quarterly.

**State Agencies Affected:** Department of State Revenue; Indiana Education Savings Authority.

**Local Agencies Affected:** County Airport Authorities; Ft. Wayne Airport Authority.

**Information Sources:** Department of State Revenue, Sales Tax database.

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