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FISCAL IMPACT STATEMENT

LS 6943
BILL NUMBER: SB 236

NOTE PREPARED: Jan 1, 2010
BILL AMENDED:

SUBJECT: State Tax Matters.

FIRST AUTHOR: Sen. Hershman
FIRST SPONSOR:

BILL STATUS: As Introduced

FUNDS AFFECTED: GENERAL
DEDICATED
FEDERAL

IMPACT: State

Summary of Legislation: *Internal Revenue Code Reference Update:* The bill amends the definition of federal "Internal Revenue Code" used in Indiana statutes and regulations to refer to the Internal Revenue Code in effect on January 1, 2010. It requires that two years be used for the net operating loss carryback period for taxpayers (instead of the five years allowed under the federal Worker, Homeownership, and Business Assistance Act of 2009).

Electronic Filing of Tax Withholding Forms: The bill requires that federal income tax withholding statements and annual withholding tax reports must be filed electronically with the Department of State Revenue if an employer or a person or entity acting on behalf of an employer files more than 25 federal income tax withholding statements with the Department in the calendar year.

Patent Income Exemption: The bill provides that a taxpayer may not claim the patent income exemption with respect to a particular qualified patent unless the first taxable year in which the exemption is claimed begins before January 1, 2011.

Tax Credit Sunsets: The bill expires the teacher summer employment tax credit on January 1, 2011. It provides that an Enterprise Zone loan interest credit may not be awarded for interest received on a qualified loan made after December 31, 2010. It also expires the neighborhood assistance credit on January 1, 2011. The bill specifies that maternity home tax credit may not be awarded for the providing after December 31, 2010, of a temporary residence. It provides that an Enterprise Zone investment cost tax credit may not be awarded for a qualified investment made after December 31, 2010. It provides that a community revitalization enhancement district tax credit may not be awarded for a qualified investment made after December 31, 2010. It provides that a tax credit may not be awarded for making available after December

31, 2010, a health benefit plan. It also provides that a small employer qualified wellness program tax credit may not be awarded for costs incurred after December 31, 2010.

Effective Date: November 6, 2009 (retroactive); January 1, 2010 (retroactive); July 1, 2010.

Explanation of State Expenditures: *Electronic Filing of Tax Withholding Forms:* The bill requires an employer to electronically file employee W-2 forms and the WH-3 form with the Department of State Revenue (DOR) in any calendar year that the employer files more than 25 W-2 forms with the DOR. This requirement also applies to a person or entity such as a payroll company that files these forms on behalf of an employer. The electronic filing requirement begins in 2011. The requirement is expected to result in a cost savings to DOR by significantly reducing the number of paper W-2 and WH-3 forms that must be imaged and stored and by reducing manual data entry from the paper forms.

The W-2 is an Internal Revenue Service form on which an employer annually files reporting wages, salaries, and other compensation paid to an employee and the federal, state, and local income taxes and FICA taxes withheld on the compensation. The WH-3 is a DOR form that an Indiana employer must submit along with W-2s reporting the state income tax and local option income tax withheld by the employer, including county-by-county breakdown of local option income tax withholdings.

Tax Exemption/Credit Changes: DOR would incur some administrative expenses relating to the revision of tax forms, instructions, and computer programs to reflect the changes to exemptions and credits proposed in the bill. The DOR's current level of resources should be sufficient to implement these changes.

Explanation of State Revenues: *Internal Revenue Code Reference Update:* The bill updates the reference to the Internal Revenue Code (IRC) to incorporate all the federal changes made up to January 1, 2010. The current reference to the IRC pertains to all IRC provisions amended and in effect on February 17, 2009. The update would include changes as a result of the *Worker, Homeownership, and Business Assistance Act of 2009* (P. L. 111-92), signed into law on November 6, 2009. This federal act should not generate a material fiscal impact because the bill decouples from provisions of the federal act allowing a special 5-year (instead of 2-year) carryback for 2008 and 2009 net operating losses incurred by businesses.

Patent Income Exemption: The bill prohibits a taxpayer from claiming the patent-derived income exemption with respect to a patent unless the exemption was initially claimed prior to January 1, 2011. This exemption was first effective in tax year 2008. Preliminary data for tax year 2008 indicates that 5 individual taxpayers claimed exemptions totaling \$26,216, and 10 corporate taxpayers claimed exemptions totaling \$43,276.

The exemption applies to income derived by an individual or corporate taxpayer from utility patents or plant patents issued after December 31, 2007. The income can be from: (1) licensing fees or other income received for the use of a patent; (2) royalties received for the infringement of a patent; (3) receipts from the sale of a patent; and (4) certain income from the taxpayer's own use of the qualified patent to produce the claimed invention. A taxpayer may claim the exemption for 10 years with respect to a particular patent. The total exemption amount that a taxpayer may claim in a taxable year is \$5 M.

Tax Credit Sunsets: The bill sunsets the income tax credits as described below. The two tables following the explanation of the credit provisions report the number of individual and corporate taxpayers claiming each credit in 2005, 2006, and 2007, and the total credit amount claimed each year.

(1) Teacher Summer Employment Compensation Credit: The bill eliminates the tax credit after December

31, 2010. This is a nonrefundable tax credit that may be claimed by an individual or corporate taxpayer employing a teacher in a qualified position during school summer recess. The credit is equal to the lesser of 50% of the compensation paid to the teacher during the taxable year or \$2,500.

(2) Enterprise Zone (EZ) Loan Interest Credit: The bill prohibits the tax credit from being awarded for interest on loans made after December 31, 2010. This is a nonrefundable tax credit that may be claimed by an individual or corporate taxpayer for interest income earned by the taxpayer from a loan that directly benefits an EZ business, increases EZ property values, or is used to rehabilitate, repair, or improve an EZ residence. The credit is equal to 5% of the loan interest received during the taxable year.

(3) Neighborhood Assistance Credit: The bill eliminates the tax credit after December 31, 2010. This is a nonrefundable tax credit that may be claimed by an individual or corporate taxpayer contributing to individuals, groups, or neighborhood organizations, or engaging in activities to upgrade economically disadvantaged areas for economically disadvantaged households. The credit is limited to the lesser of 50% of the amount contributed or invested during the taxable year or \$25,000. Total credits awarded during any state fiscal year is limited to \$2.5 M.

(4) Enterprise Zone Investment Cost Credit: The bill prohibits the tax credit from being awarded for investment made after December 31, 2010. This is a nonrefundable tax credit that may be claimed by an individual or corporate taxpayer purchasing an ownership interest in an EZ business. The credit varies depending on the type of investment, the type of business, and the number of jobs created. The maximum credit is 30% of the qualified investment.

(5) Maternity Home Tax Credit: The bill prohibits the tax credit from being awarded for providing residence in a maternity home after December 31, 2010. This is a nonrefundable tax credit that may be claimed by a taxpayer owning and operating a registered maternity home that provides a temporary residence for at least 60 days to an unrelated pregnant woman. The maximum credit is \$3,000 for a taxable year. Total credits awarded during any state fiscal year is limited to \$500,000.

(6) Community Revitalization Enhancement District (CRED) Tax Credit: The bill prohibits the tax credit from being awarded for investment made after December 31, 2010. This is a nonrefundable tax credit that may be claimed by an individual or corporate taxpayer making qualified investment for the redevelopment or rehabilitation of property located within a CRED. The credit is equal to 25% of the qualified investment during the taxable year.

(7) Credit for Offering Health Benefit Plans: The bill prohibits the tax credit from being awarded for the provision of a health benefit plan after December 31, 2010. This is a nonrefundable tax credit that may be claimed in each of the first two years that an employer makes a health benefit plan available to employees. The credit is equal to \$50 per employee enrolled in the employer's health benefit plan, up to a maximum of \$2,500 per year in each of the first two years the plan is offered. An employer claiming the credit must offer health insurance for at least 24 consecutive months after the taxable year in which the health benefit plan is initially offered.

(8) Small Employer Qualified Wellness Program Credit: The bill prohibits the tax credit from being awarded for wellness program costs incurred after December 31, 2010. This is a nonrefundable tax credit that may be claimed by an employer providing a qualified employee wellness program certified by the Indiana State Department of Health. The tax credit is equal to 50% of the cost incurred by the taxpayer to provide the wellness program during the taxable year.

| Individual Income Taxpayers | 2005 | 2006 | 2007 |
|---|-------------|-------------|-------------|
| Teacher Summer Employment Compensation Credit | | | |
| Taxpayers Claiming Credit | 17 | 22 | 21 |
| Credits Claimed | \$14,262 | \$11,917 | \$15,855 |
| Enterprise Zone Loan Interest Credit | | | |
| Taxpayers Claiming Credit | 28 | 21 | 72 |
| Credits Claimed | \$71,096 | \$12,944 | \$76,630 |
| Neighborhood Assistance Credit | | | |
| Taxpayers Claiming Credit | 3,895 | 3,208 | 3,488 |
| Credits Claimed | \$2,287,740 | \$1,415,197 | \$2,232,736 |
| Enterprise Zone Investment Cost Credit | | | |
| Taxpayers Claiming Credit | 11 | 7 | 40 |
| Credits Claimed | \$151,875 | \$22,071 | \$171,502 |
| Maternity Home Tax Credit | | | |
| Taxpayers Claiming Credit | 10 | 15 | 13 |
| Credits Claimed | \$3,914 | \$6,615 | \$4,718 |
| Community Revitalization Enhancement District Tax Credit | | | |
| Taxpayers Claiming Credit | 94 | 84 | 55 |
| Credits Claimed | \$291,249 | \$54,228 | \$416,447 |
| Credit for Offering Health Benefit Plans* | | | |
| Taxpayers Claiming Credit | | | 214 |
| Credits Claimed | | | \$137,189 |
| Small Employer Qualified Wellness Program Credit* | | | |
| Taxpayers Claiming Credit | | | 83 |
| Credits Claimed | | | \$81,631 |
| *Effective beginning in tax year 2007. | | | |

| Corporate Income Taxpayers | 2005 | 2006 | 2007 |
|---|-------------|-------------|-------------|
| Teacher Summer Employment Compensation Credit | | | |
| Taxpayers Claiming Credit | N/A | 1 | 1 |
| Credits Claimed | N/A | \$2,500 | \$2,500 |
| Enterprise Zone Loan Interest Credit | | | |
| Taxpayers Claiming Credit | 28 | 28 | 20 |
| Credits Claimed | \$2,291,921 | \$2,441,498 | \$2,490,933 |
| Neighborhood Assistance Credit | | | |
| Taxpayers Claiming Credit | 41 | 18 | 16 |
| Credits Claimed | \$42,956 | \$26,450 | \$19,050 |
| Enterprise Zone Investment Cost Credit | | | |
| Taxpayers Claiming Credit | N/A | 0 | 1 |
| Credits Claimed | N/A | \$0 | \$1,358 |
| Maternity Home Tax Credit | | | |
| Taxpayers Claiming Credit | N/A | 0 | 0 |
| Credits Claimed | | \$0 | \$0 |
| Community Revitalization Enhancement District Tax Credit | | | |
| Taxpayers Claiming Credit | N/A | 3 | 3 |
| Credits Claimed | N/A | \$623,539 | \$2,663,171 |
| Credit for Offering Health Benefit Plans* | | | |
| Taxpayers Claiming Credit | | | 2 |
| Credits Claimed | | | \$2,550 |
| Small Employer Qualified Wellness Program Credit* | | | |
| Taxpayers Claiming Credit | | | 9 |
| Credits Claimed | | | \$20,681 |
| N/A=Data not available for 2005. *Effective beginning in tax year 2007. | | | |

Explanation of Local Expenditures:

Explanation of Local Revenues: The bill would limit the potential reductions in taxable income after 2010 from the patent income exemption. This would limit potential future revenue loss from this exemption to counties imposing local option income taxes. The precise impact is indeterminable at this point.

State Agencies Affected: DOR.

Local Agencies Affected: Counties with local option income taxes.

Information Sources: Tom Conley, DOR, 317-232-2107. OFMA Income Tax databases 2005-2007.

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