LEGAL UPDATE

Legal Services Division

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Ground Floor, State Capitol Building | Des Moines, Iowa 50319 | 515.281.3566

TAX CREDIT REVIEW COMMITTEE MEETING — OCTOBER 30, 2019

Purpose. *Legal updates are prepared by the nonpartisan Legal Services Division of the Legislative Services Agency. A legal update is intended to provide legislators, legislative staff, and other persons interested in legislative matters with summaries of recent meetings, court decisions, Attorney General Opinions, regulatory actions, federal actions, and other occurrences of a legal nature that may be pertinent to the General Assembly's consideration of a topic. Although an update may identify issues for consideration by the General Assembly, it should not be interpreted as advocating any particular course of action.*

Co-chairperson: Senator Jake Chapman
Co-chairperson: Representative Lee Hein

Overview. The Tax Credit Review Committee was established in 2018 Iowa Acts, chapter 1161 (SF 2417). Co-chairperson Hein and Co-chairperson Chapman commented that the committee was created to learn and gather more information about tax credits.

State General Fund Tax Credits. Mr. Jeff Robinson, Senior Legislative Analyst, Legislative Services Agency, provided historical background information related to the development of tax credits and to the present-day use and growth of such credits. He stated there was no "economic development" subtitle in the Iowa Code in 1983 and there were 20 sales tax exemptions. Today, state government is involved in economic development and there are 106 sales tax exemptions. He noted the following Iowa-specific tax credits or deductions were available in 1983: the child and dependent care tax credit; individual taxpayer, dependent, age 65 plus, and blind tax credits; and the adoption expense deduction. The first significant tax credits were enacted during the 1983 Legislative Session in response to a recession, and included a job training tax credit, a venture capital fund investment credit, and a research activities tax credit. The tuition and textbook tax credit was created in 1987. During the 1989 Legislative Session, the state earned income tax credit and the new jobs tax credit were created by the General Assembly. In 1994, the General Assembly created Quality Jobs Enterprise Zones and the New Jobs and Income Program. The New Jobs and Income Program was replaced by the High Quality Jobs Program in 2005. Other significant tax credits created in the previous 20 years include the redevelopment tax credit, the biodiesel blended fuel tax credit, the wind energy production tax credit, the school tuition organization tax credit, the endow Iowa tax credit, and the historic preservation tax credit. Mr. Robinson stated tax credits reduced state revenues by $373 million for FY 2019 and overall state revenues have been reduced by $4.235 billion between FY 2005 and FY 2019.

Tax Credit Mechanics. Dr. Amy Rehder Harris, Research Policy Division Administrator, Department of Revenue, stated that Iowa has 31 tax credits to claim against income tax returns, plus 5 tax credits where the program has been expired but claims have been made in the prior three years. She suggested classifying tax credits into three concepts: awarded, automatic, and administrative. Awarded tax credits require the taxpayer to apply with a state agency prior to doing any work and making a claim. There are 18 awarded tax credits in Iowa, and awarded tax credits are frequently capped. Automatic tax credits may be claimed on the income tax return by any eligible taxpayer completing a form that describes eligibility and calculates the tax credit. There are 13 automatic tax credits in the Iowa Code. Administrative tax credits are tax credits to avoid double taxation. There are five administrative tax credits.

Tax credits may also be refundable or nonrefundable. If a tax credit is nonrefundable, the tax credit may only be used to reduce Iowa income tax liability to $0 but not below $0. If a tax credit is refundable, and the refundable credits reduce income tax liability below $0, the Department of Revenue issues a refund to the taxpayer consisting of the remaining balance of the tax credit not used to reduce income tax liability. For FY 2019, refundable tax credits totaled $211 million and nonrefundable tax credits totaled $118 million.

There are six awarded tax credits that are transferable. A transferable tax credit allows a taxpayer awarded a tax credit to sell the tax credit to another taxpayer. Many tax credits also remain unclaimed by a taxpayer, or taxpayers are put on waitlists to claim the tax credit in future tax years. Dr. Harris noted that 24 percent of high quality jobs tax credits expire and are never claimed and 6.5 percent of endow Iowa tax credits go unclaimed.

Contingent Liabilities Report and the State Budget. Ms. Angela Gullickson, Senior Fiscal and Policy Analyst, Department of Revenue, discussed the Contingent Liabilities Report issued by the Department of Revenue. The report tracks and analyzes tax credits with the goal of providing a repository for information concerning the awarding, usage, and effectiveness of tax credits. The first contingent liabilities report was published in 2007. The most recent report forecasts 37 tax credits including expected future claims projections. There are 20 capped tax credits forecast each year. There are five expired tax credits that continue to be forecast due to carryforward credits rolling in after the expiration of the program.

Income Tax Credit Evaluations. Dr. Harris stated that Iowa has completed 37 income tax credit evaluations since 2007. Most tax credit evaluations are done in conjunction with the Tax Expenditure Committee established in Iowa Code section 2.48. When a tax credit is evaluated within the Department of Revenue, an advisory panel is created to help complete a thorough, unbiased review. The panel consists of program administrators, stakeholders, and academics. The advisory panel meets three times during the review process. The review compares similar programs across states and the federal government, reviews statistics on tax credit claimants, and performs economic analysis of the tax credit. Pew Charitable Trusts cites Iowa's evaluation process as a leader among the states.

Tax Credit Sunsets and the State Budget. Mr. Michael Mertens, Policy Director for Pass-Through Entities, Department of Revenue, stated that when a tax credit is repealed, the state should consider the following prior to repeal: whether a tax credit award is memorialized in contract between a state agency and a taxpayer; whether multiyear performance by a taxpayer may be required prior to the issuance of a tax credit; and the impact on existing contracts. If a tax credit is repealed, and in addition to the fiscal impact and contract considerations, the General Assembly should address transferability, carryforwards, and waitlists.

Committee Discussion. The committee discussed whether another meeting should be scheduled and whether a more formal review of tax credits during each legislative session would be beneficial.

LSA Staff: Joseph McEniry, Legal Services, 515.281.3189, joseph.mceniry@legis.iowa.gov; Kate O'Connor, Legal Services, 515.281.6329, kate.oconnor@legis.iowa.gov.

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