



SF 576 – Trigger Repeal and Inheritance Tax (LSB2794SV.1)
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Fiscal Note Version – Revised (Fiscal Impact)

Description

Senate File 576 contains two actions. The Bill:

- Strikes 2018 Iowa Acts, chapter **1161**, section 133 (contingent income tax system trigger requirements), and replaces the section with an unqualified effective date of January 1, 2023.
- Phases out and then repeals the inheritance tax and the qualified use inheritance tax. The changes are effective upon enactment and apply retroactively to deaths occurring on or after January 1, 2021.

Background

Division I — Contingent Income Tax System Triggers

2018 Iowa Acts, chapter 1161, Division IX, made future changes to how Iowa individual income tax liability is calculated. The effective date of Division IX of the 2018 legislation is contingent upon Iowa General Fund revenue reaching two revenue targets, or triggers, at the conclusion of a fiscal year. The two triggers are:

- Actual General Fund net revenue for the fiscal year equals or exceeds \$8,314,600,000.
- Actual General Fund net revenue for the fiscal year equals or exceeds 104.0% of the actual General Fund net revenue for the previous fiscal year.

Under the provisions of section 133 of the 2018 legislation, the first year that the two targets may be met is FY 2022, and the first year that the changes in Division IX may become effective is tax year (TY) 2023.

At the March 2021 meeting of the Revenue Estimating Conference (REC), the REC established an FY 2022 General Fund estimate of \$8,385.6 million and a growth rate of 3.8% compared to the FY 2021 estimate of \$8,078.9 million. The FY 2022 revenue projection is therefore \$71.0 million above the dollar trigger but 0.2 percentage points below the required 4.0% growth trigger. The REC projection does not mean that both triggers will not or cannot be met at the conclusion of FY 2022, but it does mean that the triggers are not projected to be met for FY 2022 at this time.

Division II — Inheritance Tax

Inheritances received by a spouse or lineal ascendants and descendants (children, grandchildren, parents, grandparents, etc.) are exempt from Iowa inheritance tax under current law. For inheritances not exempt, the tax rate varies by size of the inheritance and category of inheritor.

- If the net value of the entire estate is less than \$25,000, the tax rate is 0.0%.
- For a brother, sister, son-in-law, or daughter-in-law, the rate is 5.0% to 10.0%.
- For an aunt, uncle, niece, nephew, foster child, cousin, brother-in-law, sister-in-law, and all other individual persons, the rate is 10.0% to 15.0%.
- For firms and for-profit corporations and organizations, the rate is 15.0%.

- For charitable, educational, or religious organizations organized under the laws of any other state or country, the rate is 10.0%.
- For bequests for religious services in excess of \$500, the rate is 10.0%.
- For unknown heirs, the rate is 5.0%.
- For public libraries and art galleries, hospitals, humane societies, municipal corporations, or for the care of cemetery or burial lots, or bequests for religious services not to exceed \$500, the rate is 0.0%.

The State qualified use inheritance tax may apply to certain property of the decedent that was used in farming or other trade or business.

Assumptions

Division I — Contingent Income Tax System Triggers

- The first fiscal year both triggers may be met under current law is FY 2022, and if both triggers are met that year, the contingent income tax system becomes effective for TY 2023 and after. However, in March 2021, the REC established a FY 2022 revenue estimate that does not achieve both triggers at the conclusion of that fiscal year. Therefore, this projection assumes FY 2023 will be the first year that both triggers are met and that the contingent income tax system will become effective for TY 2024 and after.
- The Department of Revenue utilized the individual income tax micromodel to calculate the tax reduction associated with the change to the contingent income tax system for TY 2023. The fiscal impact was determined by comparing model results of tax liability under current law (existing individual income tax system for TY 2023) versus tax liability under the Bill (contingent income tax system for TY 2023). Although removing the triggers only directly changes the tax system for one year (TY 2023), the change also has a projected impact in TY 2024 as taxpayers adjust for federal tax payments made and refunds received in TY 2024 that relate to TY 2023 and before. The change also has an ongoing impact on income tax brackets as the brackets are established in the contingent system as specific income levels that are then indexed each tax year after the first implementation year. Implementing the contingent tax system one year earlier will mean that tax brackets are lower by one year's worth of indexing for all future years. The Department model estimates the TY 2023 change will reduce State individual income tax liability by the following amounts:
 - TY 2023 = \$297.6 million
 - TY 2024 = \$43.7 million
 - TY 2025 and after = \$8.0 million per tax year
- The tax year impacts are assumed to be distributed 52.0% to the fiscal year that ends during the tax year through reduced withholding and estimate payments and 48.0% to the succeeding fiscal year through reduced withholding, estimate payments, payments with tax returns, and increased tax refunds.
- The reduction in State income tax liability will reduce the amount raised by the local option income surtax for schools by 3.0% of State income tax reduction.
- Other changes made within the contingent income tax system (2018 Iowa Acts, chapter 1161, sections 128 through 130) are projected to reduce FY 2024 corporate income tax liability by \$17.9 million and bank franchise tax liability by \$2.0 million.

Division II — Inheritance Tax

- For FY 2021 and FY 2022, the assumed amount of revenue the State will receive under current law is equal to the December 2020 REC gross inheritance tax estimates for those years.
- For years beyond FY 2022, inheritance tax revenue is projected to grow 3.5% per year under current law.

- Annual estimates of gross inheritance tax receipts are reduced \$2.5 million to adjust for the average annual amount of gross inheritance tax that is refunded.
- Inheritance tax returns and payment are due nine months after the death date. Therefore, the revenue impact of the phaseout changes is delayed nine months.
- Future payments from deferred life estates and remainder interests, due from inheritances received prior to the repeal of the inheritance tax, are assumed to be minor and are therefore ignored in the fiscal impact calculation.

Fiscal Impact

The repeal of the contingent income tax system triggers and the phaseout of the Iowa inheritance tax are projected to reduce General Fund revenue by the annual amounts listed below.

Projected General Fund Revenue Change by Tax Type and Fiscal Year					
In Millions					
	Trigger Individual Income Tax	Trigger Corporate Income Tax	Trigger Bank Franchise Tax	Inheritance Tax	Total
FY 2022	\$ 0.0	\$ 0.0	\$ 0.0	\$ -17.9	\$ -17.9
FY 2023	-154.6	0.0	0.0	-40.8	-195.4
FY 2024	-160.2	-17.9	-2.0	-65.3	-245.4
FY 2025	-30.1	0.0	0.0	-91.5	-121.6
FY 2026	-8.4	0.0	0.0	-98.8	-107.2
FY 2027	-8.0	0.0	0.0	-102.3	-110.3

The revenue reduction will continue past FY 2027 at a similar level to FY 2027. The trigger repeal is also projected to reduce the revenue raised by the local option income surtax for schools by a total of \$10.8 million over the five fiscal years.

Sources

Department of Revenue
Inheritance tax receipts and refunds history

/s/ Holly M. Lyons

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The fiscal note for this Bill was prepared pursuant to [Joint Rule 17](#) and the Iowa Code. Data used in developing this fiscal note is available from the Fiscal Services Division of the Legislative Services Agency upon request.