# AN ANALYSIS OF THE IMPACT ON IOWA
# OF
# THE TAX EQUITY AND FISCAL RESPONSIBILITY
# ACT OF 1982



PREPARED BY
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# FOREWORD

This paper prepared by the Iowa Department of Revenue examines the Tax Equity and Fiscal Responsibility Act of 1982 and its impact on Iowa tax receipts. Estimating techniques which are consistent with those used in examinations of the 1981 federal legislation have been utilized.

This examination is based on the assumption that relevant changes in the Internal Revenue Code are adopted for Iowa tax purposes. Actual legislative proposals may provide for additional adjustments in state law that limit or extend the effect of the federal changes.

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## I. INTRODUCTION

The recently enacted federal tax legislation, the Tax Equity and Fiscal Responsibility Act of 1982, includes a number of provisions which will directly change the state tax liability of many individual and corporate Iowa income taxpayers. In addition, the federal legislation contains increases in excise taxes and unemployment taxes which will directly and indirectly affect the state's taxpayers.

This analysis focuses primarily on the federal income tax revisions which may alter Iowa tax liabilities in two distinct ways. First, certain of the federal changes will become part of Iowa tax law base if references to the Internal Revenue Code are adopted. Secondly, since Iowa law allows for the deduction of federal taxes when computing Iowa tax liabilities, a change in federal taxes will often result in a change in state tax liabilities.

In addition to the provisions examined, other features of the legislation may be significant in individual cases. However, it is felt that the provisions selected will affect the tax situation of more taxpayers than the provisions which were excluded. Specifically excluded are the provisions which are intended to increase compliance other than withholding and state tax refund reporting, the revisions in insurance taxation and those miscellaneous provisions aimed at specific industries or taxpayers.

The examination concentrates on the impact of the changes in fiscal 1984 and 1985. However, where possible, effects in fiscal 1983 are provided. Further, it should be noted that the impact of several of the provisions in the years after 1985 may be significantly less or greater than the stated effect presented in this paper.

This report continues with a review of the general assumptions and limitations which are associated with the estimates of the fiscal effects. Next, is a summary of the Iowa impact of seventeen specific changes. A detailed analysis of each of the selected provisions is then presented. For each of the revisions, there is a brief explanation of the current law, a description of the revised federal legislation and a review of the Iowa fiscal and administrative impact of the provision assuming conformance of the state law with the federal legislation.

## II. GENERAL ASSUMPTIONS

Completion of the estimates required that several significant assumptions be made. The accuracy of the estimates shown is dependent on the validity of these assumptions.

1. The analysis is based on the assumption that Iowa tax laws will conform with federal legislation and that additional adjustments in state law to offset or accentuate the effect of the federal changes will not

be made. It is recognized that for some of the provisions that the state may elect to consider alternatives to simple conformity which would alter the stated revenue effects. The impact of each of these alternatives should be separately examined.

2. The accuracy of the estimates are dependent to a great extent on the validity of the estimates of the federal tax impact prepared by a variety of sources including the U. S. Joint Committee on Taxation. Revisions in the estimates of the federal impact may necessitate adjustments in the current projections of the state impact.

3. The basic projections of the national effects from which many of the state estimates were derived reflect changes expected in the nation's economy. To the extent the economic recovery in Iowa varies in degree and timing from the national economy, the estimates provided would be subject to revision.

4. Estimates are provided for the biennium ending in fiscal 1985. The impact of certain provisions in years beyond fiscal 1985 could differ significantly from those shown.

## III. SUMMARY OF PROVISIONS AND IMPACT

The projected impact of the federal law changes reflect assumptions that Iowa statutes will conform with federal legislation. The dollar impact and the associated timing would be expected to vary if an alternative to conformance was adopted.

Examination of the accompanying summary table on pages 5 and 6 reveals:

(1) The impact on Iowa receipts in fiscal 1983 results from a one-half million dollar decrease indirectly occurring because of the change in federal cigarette tax rate and a $2.0 million to $3.0 million increase in individual income tax collections from additional taxation of unemployment benefits.

(2) An expected increase in Iowa receipts from the provisions estimated totalling $15.3 million to $20.3 million in fiscal 1984 with a large part of this increase resulting from changes in individual income tax medical itemized deductions.

(3) Fiscal 1985 receipts would be increased by $15.0 million to $21.5 million.

(4) Among the provisions for which no Iowa estimate is shown are changes in leasing rules, federal withholding on interest, dividends and pensions and changes in pension rules. These estimates are not presented generally because all require consideration of unique Iowa circumstances which need further study.

ADOPTION OF SELECTED PROVISIONS
TAX EQUITY AND FISCAL RESPONSIBILITY
ACT OF 1982
IOWA TAX IMPACT
FISCAL YEARS 1983, 1984 AND 1985
(Dollars in Millions)

| Provision | Fiscal 1983 | Fiscal 1984 | Fiscal 1985 |
|---|---|---|---|
| A. Individual Income Tax Revisions | | | |
| 1. Individual Alternative Tax | None | +$1.8 | +$1.5 |
| 2. Itemized Deduction For Medical Expenses | None | +$7.0 to +$9.0 | +$4.5 to +$6.5 |
| 3. Itemized Deductions for Nonbusiness Casualty and Theft Losses | None | +$1.0 | +$1.0 |
| 4. Withholding on Interest and Dividends and Certain Pensions and Annuities | None | Further analysis required | |
| 5. Taxation of Unemployment Benefits | +$2.0 to +$3.0 | +$1.0 to +$2.0 | +$1.0 to +$2.0 |
| 6. Pension Plan Revisions | None | No estimate of increase possible | |
| 7. Reporting of State and Local Income Tax Refunds | None* | None* | None* |
| B. Business Income Tax Changes | | | |
| 1. Reduction in Corporate Tax Preferences | None | +$1.0 | +$1.0 |
| 2. Investment Tax Credit Basis Adjustment | Minimal Increase | +$2.0 to +$2.5 | +$3.5 to +$4.5 |
| 3. Investment Tax Credit Limitation | None | Minimal Reduction | Minimal Reduction |

*State expenditures of $100,000 annually

| Provision | Fiscal 1983 | Fiscal 1984 | Fiscal 1985 |
|---|---|---|---|
| 4. Change in ACRS Schedules for 1985 and After | None | None | +$1.0 to +$2.0 |
| 5. Construction Period Interest and Taxes | Minimal Increase | +$1.0 to +$2.0 | +$1.0 to +$2.0 |
| 6. Revision in Leasing Rules | Further analysis required | | |
| 7. Extension and Revision of Jobs Credit | None | Minimal Increase | Minimal Increase |
| C. Excise Tax Provisions | | | |
| 1. Airport and Airway Taxes | None | None | None |
| 2. Cigarette Tax Increase | -$.5 | +$.5 to +$1.0 | +$.5 to +$1.0 |
| 3. Telephone Excise Tax | None | None | None |
| Sum of Estimated Total Impact of Selected Provisions | +$1.5 to +$2.5 million | +$15.3 to $20.3 million | +$15.0 to $21.5 million |

# INDIVIDUAL ALTERNATIVE TAX

## I. Explanation of Change

### A. Current Law

Federal - Individuals, estates and trusts may be subject to two minimum taxes on some tax preferences. "Tax preferences" are certain deductions that have been used to reduce income subject to tax. One minimum tax is called the "add-on minimum tax", and the other is the "alternative minimum tax".

(1) "Add-on minimum tax" is 15 percent of the total of certain tax preferences in excess of $10,000 or one-half of the taxpayer's tax liability. Tax preferences considered in this calculation include some accelerated depreciation schedules, depletion allowances, rapid amortization and intangible drilling costs.

(2) "Alternative minimum tax" is applicable only if capital gains deductions and/or certain itemized deductions are taken. The tax is imposed only to the extent that it exceeds the taxpayers regular tax and the add-on minimum tax.

Iowa - The Iowa tax is twenty-five percent of any applicable federal add-on or alternative minimum tax.

B. New Provision

(1) The add-on minimum tax is repealed.

(2) The alternative minimum tax is broadened to prevent avoidance of all tax liability as the result of taking certain deductions from income. The deductions to be considered include most of the tax preferences in the previous add-on and alternative taxes plus some additional ones including certain interest and dividend exclusions.

(3) The first $30,000 of income adjusted for tax preferences ($40,000 on a joint return) is exempt from the tax.

(4) The tax rate is a uniform 20 percent and is imposed only to the extent that the alternative tax exceeds regular tax liability.

C. Effective Date for Federal Impact - Tax years beginning in 1983.

II. Impact on Iowa if IRC Update Adopted

A. Nature of Impact - Iowa individual income tax revenues will increase. The increase will be somewhat modified by larger federal tax deductions starting in fiscal 1985.

B. Effective Date of the Impact in Iowa - The impact will be first noticed when tax year 1983 returns are filed in fiscal 1984.

C. Revenue Impact -

| Fiscal Year | |
|---|---|
| 1983 | None |
| 1984 | Increase - $1.8 million |
| 1985 | Increase - $1.5 million |

D. Administrative Impact - None.

## ITEMIZED DEDUCTION FOR MEDICAL EXPENSES

I. Explanation of Change

A. Current Law - Itemized deductions may be taken for medical expenses in excess of 3 percent of adjusted gross income. A separate deduction for one-half (up to $150) of medical insurance premium expenses is allowed. Drug expenditures over one percent of adjusted gross income can be included in medical deductions.

B. New Provision - Four major revisions in the medical itemized deductions are adopted: (see example on page 12)

(1) Only itemized medical expenses in excess of 5 percent of adjusted gross income may be deducted.

(2) The separate medical insurance deduction is repealed.

(3) Only prescription drugs and insulin may be deducted as medicine and drug expenses.

(4) All prescription drugs and insulin expenses may be included as a medical expense starting in 1984. This repeals the one percent exclusion.

C. Effective Date for Federal Impact - Tax years beginning in 1983 except the two provisions relating to prescription drugs which are effective in 1984.

II. Impact on Iowa if IRC Update Adopted

A. Nature of Impact - Individual income tax collections will be increased. The increase will be somewhat modified by larger federal tax deductions starting in fiscal 1985.

B. Effective Date for Impact in Iowa - The first significant impact will be when tax year 1983 individual returns are filed in fiscal 1984.

C. Revenue Impact -

| Fiscal Year | |
|---|---|
| 1983 | None |
| 1984 | Increase - \$7.0 to \$9.0 million |
| 1985 | Increase - \$4.5 to \$6.5 million |

D. Administrative Impact on Department of Revenue - None

## MEDICAL EXPENSE DEDUCTION EXAMPLES

Background:

A taxpayer who itemizes deductions and has $20,000 in adjusted gross income has the following medically related expenses for each of the years 1982 through 1984:

| | |
|---|---|
| Unreimbursed Hospital and Dental Expenses | $1,200 |
| Medical Insurance | 1,000 |
| Prescription Drug Expense | 400 |

1982 Medical Expense Deduction:

| | | |
|---|---|---|
| Hospital and Dental Expenses | | $1,200 |
| Medical Insurance | $1,000 | |
| Less Deductible Insurance | 150 | 850 |
| Drug Expense | 400 | |
| Less 1% of AGI | 200 | 200 |
| Total Medical Expenses | | $2,250 |
| Less 3% of AGI | | 600 |
| Net | | $1,650 |
| Plus: Medical Insurance Ded. | | 150 |
| Total 1982 Medical Expense | | $1,800 |

1983 Medical Expense Deduction:

| | | |
|---|---|---|
| Hospital and Dental Expenses | | $1,200 |
| Payments for Medical Insurance | | 1,000 |
| Drug Expense | $ 400 | |
| Less 1% of AGI | 200 | 200 |
| Total | | $2,400 |
| Less 5% of AGI | | 1,000 |
| Total 1983 Medical Expenses | | $1,400 |

1984 Medical Expense Deduction:

| | |
|---|---|
| Hospital and Dental Expenses | $1,200 |
| Payments for Medical Insurance | 1,000 |
| Drug Expense | 400 |
| Total | $2,600 |
| Less 5% of AGI | 1,000 |
| Total 1984 Medical Expenses | $1,600 |

ITEMIZED DEDUCTIONS FOR NONBUSINESS CASUALTY AND THEFT LOSSES

I. Explanation of Change

A. Current Law - Individuals who itemize deductions may deduct unreimbursed losses of nonbusiness property resulting from such events as fire and storms or theft. The deduction is allowed to the extent that the amount of each loss exceeds $100.

B. New Provision - Nonbusiness casualty losses will be deductible only to the extent that they exceed 10 percent of adjusted gross income. Each individual loss continues to be deductible only in excess of $100.

C. Effective Date for Federal Impact - Generally effective for tax years beginning in 1983.

II. Impact on Iowa if IRC Update Adopted

A. Nature of Impact - Individual income tax collections will be increased. Nonbusiness casualty and theft loss itemized deductions are subject to considerable fluctuation from year to year. Revenue estimates shown below should be considered as a general indication of actual impact.

B. Effective Date of the Impact in Iowa - The first significant impact will occur when tax year 1983 returns are filed in fiscal 1984.

C. Revenue Impact -

| Fiscal Year | |
|---|---|
| 1983 | None |
| 1984 | Increase - $1.0 million |
| 1985 | Increase - $1.0 million |

D. Administrative Impact on Department of Revenue - None.

WITHHOLDING ON INTEREST, DIVIDENDS
AND CERTAIN PENSIONS AND ANNUITIES

I. Explanation of Change

A. Current Law - No income tax withholding is required on payments of interest and dividends, or pension income.

B. New Provision - Two basic changes were made:

1. Interest and Dividends - Ten percent of payments of dividends and interest paid to individuals and unincorporated entities such as partnersips and estates is to be withheld. Exceptions to the withholding requirements include:

a. Individuals with prior year tax of $600 or less ($1,000 on a joint return).

b. Elderly individuals with prior year tax of $1,500 or less ($2,500 on a joint return).

c. Interest payments of $150 or less on an annual basis.

d. Payments to certain exempt recipients such as corporations and tax exempt trusts.

e. Payments by consumer cooperatives.

2. Pensions and Annuities - Payments made from a pension plan, an IRA, or a commercial annuity contract will be subject to withholding. Individuals may choose not to have tax withheld.

C. Effective Date for Federal Impact - Withholding on interest and dividends is effective for payments after June 30, 1983. Pension and annuity income is subject to withholding after December 31, 1982.

II. Impact on Iowa if IRC Update Adopted

A. Nature of Impact - Iowa tax collections are expected to increase from better reporting of interest, dividend and pension income resulting from required federal withholding. This increase will be partially offset by reduced tax collections from larger federal tax deductions.

B. Effective Date of the Impact in Iowa - Fiscal 1984.

C. Revenue Impact - Further analysis required.

D. Administrative Impact on Department of Revenue - None.

TAXATION OF UNEMPLOYMENT BENEFITS

I. Explanation of Change

A. Current Law - Unemployment insurance benefits are taxable if the total of gross income and unemployment insurance benefits exceed a base income of $20,000 for single taxpayers or $25,000 for married taxpayers filing jointly. The amount subject to tax is the lessor of:

(1) One-half of the amount by which the taxpayer's unemployment compensation plus gross income exceeds the base, or

(2) The amount of unemployment compensation.

B. New Provision - The base income amount above which a portion of unemployment insurance benefits becomes taxable is lowered to $12,000 for single taxpayers and $18,000 for married taxpayers filing jointly.

C. Effective Date for Federal Impact - Beginning with unemployment compensation paid in 1982.

II. Impact on Iowa if IRC Update Adopted

A. Nature of Impact - Iowa tax collections will increase.

B. Effective Date of the Impact in Iowa - Fiscal 1983 when tax year 1982 returns are filed.

C. Revenue Impact -

| Fiscal Year | |
|---|---|
| 1983 | Increase - \$2.0 to \$3.0 million |
| 1984 | Increase - \$1.0 to \$2.0 million |
| 1985 | Increase - \$1.0 to \$2.0 million |

D. Administrative Impact on Department of Revenue - None.

# PENSION PLAN REVISIONS

I. Explanation of Change

A. Current Law - Contributions to qualified pension plans are deductible from taxable income if the plans meet certain requirements. Different restrictions exist for HR 10 (Keogh) plans for self-employed individuals and for corporate plans.

B. New Provision - Many of the distinctions between qualified Keogh and corporate plans are eliminated. In general, Keogh plan limits are made less restrictive and corporate plan limits are made more restrictive. For instance, Keogh contributions can be as high as 25% of earned income instead of 15% and may be as large as $30,000 a year instead of $15,000. In comparison, corporate defined contribution plan payments may be as much as $30,000 annually per employee instead of $45,475.

C. Effective Date for Federal Impact - Effective dates of separate provisions vary generally beginning in 1983 and 1984.

II. Impact on Iowa if IRC Update Adopted

A. Nature of Impact - Iowa tax collections will increase.

B. Effective Date of the Impact in Iowa - First significant impact in fiscal 1984.

C. Revenue Impact -

| Fiscal Year | |
|---|---|
| 1983 | None |
| 1984 | A specific estimate of the revenue |
| 1985 | increase is not possible. |

D. Administrative Impact on Department of Revenue - None.

# REPORTING OF STATE AND LOCAL INCOME TAX REFUNDS

I. Explanation of Change

A. Current Law - No reporting required.

B. New Provision - State and local governments making refunds or allowing credits or offsets related to individual income tax must report to the Secretary of Treasury any such transaction of $10 or more. Also, a statement of the transaction must be furnished to the recipient during January of the calendar year following the year of the transaction.

C. Effective Date for Federal Impact - Transactions after 1982.

II. Impact on Iowa if IRC Update Adopted

A. Nature of Impact - Compliance is required.

B. Effective Date of the Impact in Iowa - Reporting will be on refunds issued after 1982 with the first statements to individuals in January, 1984.

C. Revenue Impact - None.

D. Administrative Impact - It is estimated that about $100,000 annually will be required for data processing, printing and postage costs.

REDUCTION IN CORPORATE TAX PREFERENCES

I. Explanation of Change

A. Current Law

Federal - Corporations in computing taxable income are allowed certain deductions which are treated as tax preferences. The tax preferences for most corporations are the amount by which certain deductions exceed the amount deductible under another method of calculation. Among the items treated as tax preferences are accelerated depreciation, depletion, rapid amortization and capital gains.

Corporations must pay a minimum tax on certain tax preferences in addition to the corporation's regular tax. The corporate minimum add-on tax rate is 15 percent of the excess of the total tax preference items over the larger of (1) the regular income tax liability after credits or (2) $10,000.

Iowa - In general Iowa allows the federal tax preferences in computing Iowa taxable income. Further, Iowa imposes a minimum tax equal to 25 percent of the federal minimum tax.

B. New Provision - Certain corporate tax preferences utilized in the calculation of taxable income are reduced by 15 percent for all corporations other than subchapter S corporations. In conjunction with this adjustment, only 71.6 percent of the tax preferences being reduced will be treated as items of tax preference under the add-on minimum tax for corporations. Also, the preference for excess amortization of child care facilities is deleted.

C. Effective Date for Federal Impact - Generally tax years beginning in calendar 1983.

II. Impact on Iowa if IRC Update Adopted

A. Nature of Impact - Corporate income tax collections will be increased as a result of the 15 percent reduction in tax preferences. Collections from the corporate minimum tax will be reduced.

B. Effective Date of the Impact in Iowa - First significant impact will be in fiscal 1984 and 1985 as corporate returns are filed for tax years beginning in calendar 1983.

C. Revenue Impact -

| Fiscal Year | |
|---|---|
| 1983 | None |
| 1984 | Increase - $1.0 million |
| 1985 | Increase - $1.0 million |

D. Administrative Impact on Department of Revenue - None.

INVESTMENT TAX CREDIT BASIS ADJUSTMENT

I. Explanation of Change

A. Current Law - Cost recovery deductions are allowed for 100 percent of the cost of a depreciable asset, including property for which the regular, energy, or historic structure rehabilitation investment tax credits are allowed. Lessors may pass through investment credits to lessees.

B. New Provision - Basis for depreciation of assets for which regular, energy, or historic structure rehabilitation investment tax credits have been taken must be reduced by 50 percent of the amount of the credit. Alternatively for the regular investment tax credit, the credit may be reduced by two percent for instance from ten to eight percent.

C. Effective Date for Federal Impact - Property placed in service after 1982.

II. Impact on Iowa if IRC Update Adopted

A. Nature of Impact - Tax collections will increase.

B. Effective Date of the Impact in Iowa - First significant impact will be in fiscal 1984.

C. Revenue Impact -

| Fiscal Year | |
|---|---|
| 1983 | Increase - Minimal |
| 1984 | Increase - \$2.0 to \$2.5 million |
| 1985 | Increase - \$3.5 to \$4.5 million |

D. Administrative Impact on Department of Revenue - None.

# INVESTMENT TAX CREDIT LIMITATION

I. Explanation of Change

A. Current Law

Federal - Investment tax credits may be used to offset the first $25,000 of tax liability plus 90% of tax liability over $25,000 except for the energy tax credit which may offset 100% of tax liability. Unused credits may be carried back three years and forward fifteen years.

Iowa - Iowa has no investment tax credit.

B. New Provision - The income tax liability in excess of $25,000 that may be offset by the investment tax credit is reduced to 85 percent except for the energy credit which may still offset 100 percent of tax. The 85 percent limit applies regardless of the year in which the investment tax credit is earned.

C. Effective Date for Federal Impact - Tax years beginning in 1983.

II. Impact on Iowa if IRC Update Adopted

A. Nature of Impact - Iowa individual and corporate income tax collections will be reduced as the result of increased federal taxes.

B. Effective Date of the Impact in Iowa - Corporate income tax collections will be reduced starting in fiscal 1984. Individual income tax collections will be reduced starting with fiscal 1985.

C. Revenue Impact -

| Fiscal Year | |
|---|---|
| 1983 | None |
| 1984 | Reduction - Minimal |
| 1985 | Reduction - Minimal |

D. Administrative Impact on Department of Revenue - None.

# CHANGE IN ACCELERATED COST RECOVERY SYSTEM SCHEDULES FOR 1985 AND AFTER

I. Explanation of Change

A. Current Law - For property put into service during calendar years 1981 through 1984, recovery of capital costs under the Accelerated Cost Recovery System approximates the amounts derived using the 150 percent declining balance depreciation method switching to the straight-line method when that is advantageous. In 1985, the schedules would accelerate to the 175 percent declining balance method switching to sum-of-the-years digits method when advantageous. For 1986 and after, the schedules were to further accelerate to a 200 percent declining balance method changing to sum-of-the-years digits when that becomes advantageous.

B. New Provision - The changes in 1985 and 1986 are repealed retaining the 1981 schedule.

C. Effective Date for Federal Impact - The change is effective for assets put in place starting on January 1, 1985.

II. Impact on Iowa if IRC Update Adopted

A. Nature of Impact - The ACRS provisions adopted in 1981 significantly reduce tax liabilities. The 1982 changes will make the impact of the 1981 changes smaller.

B. Effective Date of the Impact in Iowa - The first impact would be on estimated payments in the second half of fiscal 1985.

C. Revenue Impact - The impact shown below represents the effect in the first year of the change. The impact in subsequent years will be significantly greater.

| Fiscal Year | |
|---|---|
| 1983 | None |
| 1984 | None |
| 1985 | Increase - $1.0 to $2.0 million |

D. Administrative Impact on Department of Revenue - None.

# CONSTRUCTION PERIOD INTEREST AND TAXES

I. Explanation of Change

A. Current Law - Corporations may write-off immediately interest and taxes related to construction of commercial buildings or rental housing. Subchapter S corporations, individuals and personal holding companies must now capitalize such interest and taxes.

B. New Provision - Construction period interest and taxes will be required to be capitalized and amortized over a ten year period by all corporations for non-residential construction. Only subchapter S corporations and personal holding companies will be required to capitalize and amortize construction period interest and taxes for residential real property.

C. Effective Date for Federal Impact - Construction begun after 1982.

II. Impact on Iowa if IRC Update Adopted

A. Nature of Impact - Tax collections will increase.

B. Effective Date of the Impact in Iowa - First significant impact in fiscal 1984, although a minimal increase is possible in fiscal 1983.

C. Revenue Impact -

| Fiscal Year | |
|---|---|
| 1983 | Increase - Minimal |
| 1984 | Increase - \$1.0 to \$2.0 million |
| 1985 | Increase - \$1.0 to \$2.0 million |

D. Administrative Impact on Department of Revenue - None.

## REVISION IN LEASING RULES

I. Explanation of Change

A. Current Law

Federal - Under existing statutes whether tax benefits such as investment tax credit and depreciation have been available to the lessor of property has depended on the nature of the lease. Prior to 1981 legislation, the statutes provided a series of rules to be satisfied if the lessor was to be considered the owner of the property. These rules in effect determined that the economic substance of a transaction and not its form determined who was the actual owner of the property.

The safe harbor lease provisions enacted in 1981 permit the owners of property to transfer the tax benefits of ownership to others without having to meet the requirements for non-safe harbor leases.

Iowa - Iowa does not recognize those leases which qualify only under safe harbor provisions. However, leases qualifying under non-safe harbor provisions are recognized.

B. New Provision - As a result of the legislation, existing non-safe harbor leasing provisions have remained basically unchanged. Changes have occurred in two areas:

(1) Finance Leasing - A new form of leasing agreement has been established which is subject to many of the same restrictions as non-safe harbor leases. When an agreement qualifies as a finance lease, the lessee may have a fixed price purchase option equal to at least 10 percent of the original cost of the property, and the property need not be readily usable by others. Either of these facts will not be taken into account in determining whether the lessor is the owner of the property.

A specific form of finance leases known as "farm finance leases" takes effect for leases entered into after July 1, 1982. Certain types of farm property may qualify for finance lease treatment if the cost basis of the leased property entered into by the lessee does not exceed $150,000. Additional restrictions on farm finance leases will affect agreements entered into after 1983.

(2) Safe Harbor Leases - Revisions have been made which reduce the benefits of safe harbor leasing including changes in eligibility requirements, revisions in types of property that are eligible and

changes in benefits associated with ACRS and investment tax credit. The safe harbor provisions are repealed effective in 1984.

C. Effective Date for Federal Impact

Finance Leases - Generally effective for leases after December 31, 1983. Farm finance leases are effective for leases after July 1, 1982.

Safe Harbor - Modifications effective for property placed in service after July 1, 1982. Repealed for leases after December 31, 1983.

II. Impact on Iowa if IRC Update Adopted

A. Nature of Impact - Iowa has previously excluded consideration of safe harbor leases in determining tax liabilities. The effect of the revision and eventual repeal of safe harbor leases will depend on the extent to which pre-1981 leasing provisions, which are recognized by Iowa, are used. The impact of the finance leasing provisions will also depend on the extent to which this form of leasing is utilized as compared with the use of pre-1981 leasing and/or safe harbor leases. Further analysis is necessary before the impact both in direction and magnitude can be reliably estimated.

B. Effective Date of the Impact in Iowa - Impact could occur in fiscal 1984. However, the primary effect is expected in fiscal 1985.

C. Revenue Impact - Further analysis is required.

D. Administrative Impact on Department of Revenue - None identified.

EXTENSION AND REVISION OF TARGETED JOBS CREDIT

I. Explanation of Change

A. Current Law - For hiring of individuals from one or more of nine target groups before 1983, a credit against tax is permitted equal to 50 percent of the first $6,000 of wages paid for the first year of employment and 25 percent of the first $6,000 of wages paid for the second year of employment of each individual. The credit was due to expire at the end of 1982.

B. New Provision - The changes in the Jobs Tax Credit include:

(1) The credit is extended to hirings before 1985.

(2) A new targeted group, 16 and 17 year old disadvantaged youth, is added for summer employment in 1983 and 1984.

(3) Recipients of noncash general assistance are considered members of a target group.

(4) Eliminates as a target group individuals terminated from CETA employment.

C. Effective Date for Federal Impact - Generally effective for new employees hired after 1982.

II. Impact on Iowa if IRC Update Adopted

A. Nature of Impact - Iowa tax revenues will increase as the result of reduced federal taxes.

B. Effective Date of the Impact in Iowa - The first significant impact will be in fiscal 1984.

C. Revenue Impact -

| Fiscal Year | |
|---|---|
| 1983 | None |
| 1984 | Increase - Minimal |
| 1985 | Increase - Minimal |

D. Administrative Impact on Department of Revenue - None.

AIRPORT AND AIRWAY TAXES

I. Explanation of Change

A. Current Law - Current aviation related taxes include:

(1) A 5 percent general fund tax on air passenger tickets.

(2) A 4 cents per gallon tax on gasoline used by noncommercial aviation.

B. New Provision - The changes to aviation taxes include:

(1) The tax on air passenger tickets is increased to 8 percent.

(2) A 5 percent tax is imposed on air freight way bills.

(3) A $3 per person international departure tax is imposed.

(4) A 12 cents per gallon tax is imposed on noncommercial aviation gasoline.

(5) A 14 cents per gallon tax is imposed on other noncommercial aviation fuels.

(6) An exemption from fuel and air passenger ticket taxes is permitted for helicopters not using federally supported systems or used in timber or hard mineral exploration or development.

C. Effective Date for Federal Impact - Generally August 31, 1982.

II. Impact on Iowa

The revisions in aviation taxes will have no direct impact on state tax receipts. Further, the administration of taxes by the Department of Revenue will be unaffected.

# CIGARETTE TAX INCREASE

I. Explanation of Change

A. Current Law - A manufacturer's excise tax of 8 cents per pack or $4.00 per thousand applies to most cigarettes. Higher tax rates apply to larger cigarettes.

B. New Provision - The tax rates are doubled with a rate of 16 cents per pack on most cigarettes. An inventory tax is also imposed on the effective date.

C. Effective Date for Federal Impact - The higher taxes apply from January 1, 1983 through September 30, 1985.

II. Impact in Iowa

The increased federal cigarette tax will result in an increase in state sales tax which is imposed on the retail price of cigarettes including federal taxes. Depending on the price elasticity of demand for cigarettes the amount of cigarette taxes collected could be reduced somewhat.

The increased sales tax receipts coupled with a possible decline in cigarette consumption is expected to result in a decline in general fund revenues for fiscal 1983 of not more than $500,000. In fiscal years 1984 and 1985, the impact on general fund revenues is expected to be an increase of approximately $500,000 to $1,000,000 annually.

TELEPHONE EXCISE TAX

I. Explanation of Change

A. Current Law - A 1 percent excise tax is imposed on telephone and teletypewriter services in 1982 through 1984.

B. New Provision - A 3 percent excise tax is imposed.

C. Effective Date for Federal Impact - The tax is imposed for calendar years 1983 through 1985 and is abolished after that time.

II. Impact on Iowa

Increases in the telephone excise tax will not directly effect state tax revenues nor the administration of taxes by the Department of Revenue.