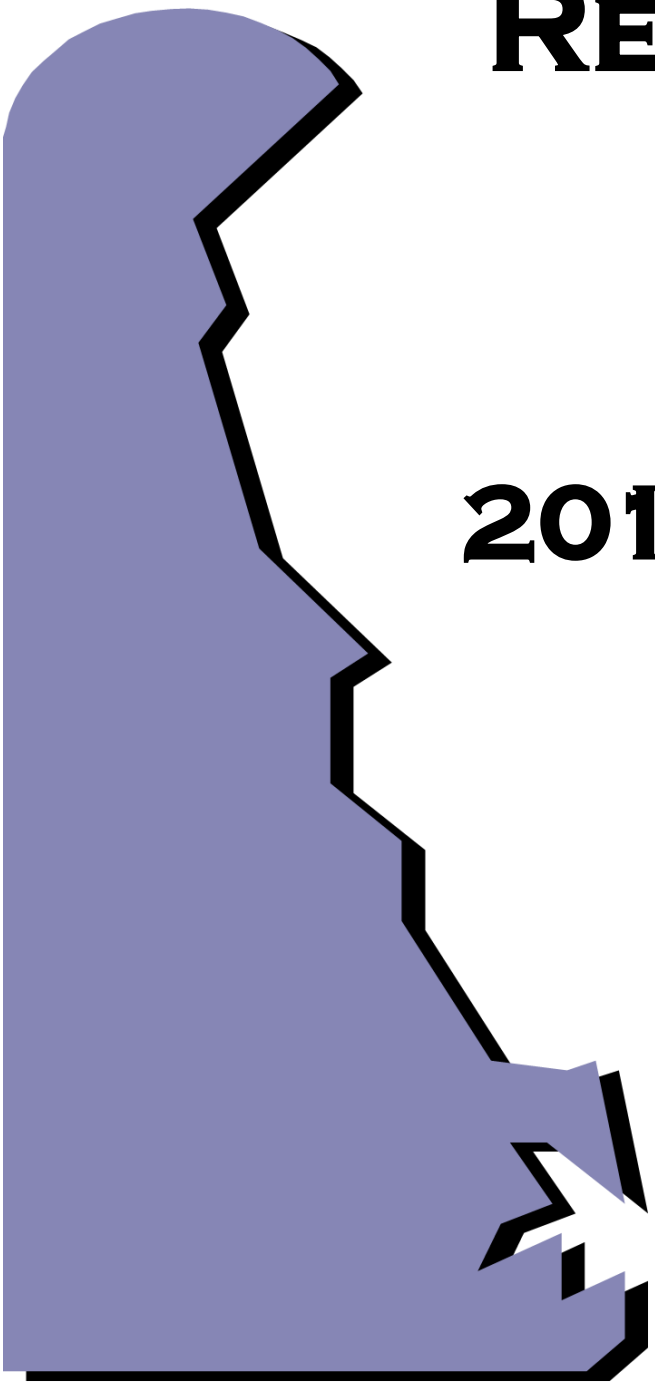
State of Delaware

Tax Preference Report



2019 Edition

DELAWARE DEPARTMENT OF FINANCE

Department of finance
Division of Revenue

EXECUTIVE SUMMARY

This Report, required by §8305(6), Title 29, Delaware Code, assesses the impact of tax preferences on the personal income tax, corporate income tax, motor fuel/special fuel tax, and public utility tax.

Tax preferences are no different from state spending in terms of their budgetary implications and are sometimes referred to as "tax expenditures." A reduction in revenues has the same fiscal impact as a direct expenditure – both consume finite public resources. Tax preferences are often established to pursue public policies that are not directly related to the tax system itself. For example, the tax-exempt status of employer-provided health insurance is primarily a health care policy that is administered through the tax system. In these cases, the effectiveness of a tax preference should be subject to the same cost-benefit analysis that direct expenditures undergo.

Using cost-benefit analysis to evaluate tax preferences is more complex than conducting similar analyses of direct expenditures. The analysis must weigh how the policy affects the tax system through which it operates. The impacts of tax preference policies are often in conflict with the goals of an "ideal" tax system. The proliferation of these policies can undermine the fairness of a tax system, erode the tax base, distort private economic incentives, and generate unnecessary complexity within the tax code.

Given their budgetary and policy equivalence to direct expenditures, the burden they may place on the tax system, and the upward trend in their use, tax preferences represent a significant component of Delaware's fiscal environment. As such, it is important that this Report receive serious attention from state policy makers.

Since the last Tax Preference Report was issued in 2017, Delaware has created three new tax preferences and expanded three existing tax preferences. A list of the tax preference changes can be found at the end of this executive summary.

ACKNOWLEDGMENTS

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The Division of Revenue would like to acknowledge the assistance, analysis and contributions of the staff of the Delaware Department of Transportation, Delmarva Power Delivery, the city of Dover, the city of Newark, and the Delaware Electric Cooperative.

The revenue estimates and judgments expressed herein, however, are ultimately those of the Division of Revenue.

Jennifer Hudson
Director of Revenue

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INTRODUCTION

Legislative Background

Title 29, Delaware Code, §8305(6) requires that the Division of Revenue, under the supervision of the Secretary of Finance, prepare biennial reports that estimate the fiscal impact of all newly enacted and existing tax preferences for selected revenue sources. Reports are due in each odd-numbered year. This sixteenth Tax Preference Report is submitted to meet the requirements of that provision for Calendar Year 2019.

The reporting of tax expenditures was incorporated into the federal budget process through the enactment of the *Congressional Budget and Impoundment Act* (CBIA) in 1974. CBIA requires the President to report on tax expenditures in the budget and requires Congressional committees to provide tax expenditure estimates for each tax bill that they report. Through this process, legislators may recognize the costs associated with tax expenditures and analyze such measures under comparable scrutiny to traditional expenditures.

Delaware took similar steps to analyze preferences within its tax system. In November 1986, a Tax Preference Report was submitted to meet the requirements of the original legislation. The Report was the state of Delaware's first published effort to identify tax preferences arising from provisions of the Delaware Code. The second Report, which the Department of Finance submitted to the General Assembly in November 1988, fulfilled the legislation's more comprehensive requirements by analyzing the impact of all state and federal tax preferences on Delaware revenues. Pursuant to Senate Bill No. 284 of the 136th General Assembly, beginning with the third Tax Preference Report – published in November 1993 – the reports have had a significantly narrower focus. Like more recent reports, this sixteenth Delaware Tax Preference Report examines statutory tax preferences within the categories of personal income tax, corporate income tax, motor fuel/special fuel tax, and public utility tax.

Purpose of the Tax Preference Report

The "Declaration of Policy" set forth in §8305(6)(a) acknowledges that state governmental policy objectives may be achieved through direct expenditures and indirectly through the use of tax preferences. Direct expenditures require annual appropriations and receive automatic, regular review through the budget process. Tax preferences do not. The primary purpose of this Report is to identify all tax preferences within specified revenue sources and assess them quantitatively and qualitatively.

A comprehensive review of tax preferences has value in its own right. Without thorough, long-term reviews, tax policy often becomes overly focused on immediate, short-term problems. In such an environment, more fundamental government goals may fall by the wayside. For example, day-to-day tax policy issues often involve the analysis of a single tax preference designed to address a particular perceived need. When viewed in isolation, a tax preference may have considerable merit and be motivated by the best of intentions. However, *ad hoc* preferences incrementally add to the complexity of the tax code and may threaten its fairness, distort decision-making, and gradually erode the tax base. Before long, the fundamental objectives of a tax system – equity, efficiency, simplicity and adequacy – may be compromised.[1]

Periodic review is necessary because time can dramatically alter the complexion of tax preferences. Tax breaks for a select and small group of people can quickly grow into expensive entitlements as demographic conditions or economic incentives induce change. Conversely, tax preferences can lose their usefulness as the income or business conditions the preferences are based on evolve.

Tax preference reports are useful tools in the annual budget process. They offer insight into foregone revenue that could be recovered, allowing budget shortfalls to be closed without resorting to tax rate increases or direct expenditure cuts. Incorporating tax preference reports directly into the budget process would enhance the visibility of these fiscal options.

The purpose of this Report is not to propose specific policy alternatives but rather to assist the tax policy debate in the state of Delaware by objectively highlighting the potential advantages and disadvantages of various tax preferences. It is our hope that this Report will help facilitate discussion of current tax preferences and the role they play in the tax system.

Components of the Tax Preference Report

As per the requirements of §8305(6), this Report provides the following information for each of the four designated tax types:

1. A description of each tax preference, its statutory basis, and its purpose.

2. An estimate of the revenue loss to the state, or one of its subdivisions, caused by each tax preference for the last fiscal year (FY 2019) and the

[1] See the section of this Report entitled "Incrementalism" below.

estimated revenue loss caused by each tax preference for the current fiscal year (FY 2020).

3. An assessment of whether each tax preference is the most fiscally effective means of achieving the purpose for which it was enacted, and whether each tax preference has been successful in meeting the purpose for which it was enacted.

4. An assessment of whether each tax preference benefits those taxpayers originally intended to benefit from it and, if not, an explanation of those who do benefit.

5. A statement of any unintended or inadvertent effects, benefits, or harm caused by each tax preference, including whether each tax preference conflicts with any other state laws, regulations, or policies.

Definition of "Tax Preference"

An essential step in preparing tax expenditure reports is defining the term "tax preference." A provision of the tax code that one onlooker considers to be grossly unfair can be a provision that another observer considers absolutely equitable and fair.

Most commentators agree that a tax preference: 1) provides a benefit only to taxpayers; 2) operates through specific statutory provisions of the tax code; and 3) depends on certain criteria, such as age, income source, or expenditure decisions that not all taxpayers meet. In general, tax expenditures are tax code provisions that narrow the tax base or give credits to certain groups of taxpayers. The federal government uses the following definition, originally found in §3(3) of the *Congressional Budget and Impoundment Act*:

> "those revenue losses attributable to provisions of the federal tax laws which allow a special exclusion, exemption, or other deduction from gross income or which provide a special credit, a preferential rate of tax, or a deferral of tax liability."

The tax base for both the federal and state income tax is "net income" in the case of corporate income tax and "adjusted gross income" in the case of personal income tax. In either case, the base equals gross income less certain costs. Not all subtractions from "net income" can be called tax preferences. For example, costs of earning income are

often deductible, but they are not considered tax preferences. These expenses are deductible by all taxpayers, so no preferential treatment occurs.

In addition, certain features of the tax code are considered integral parts of its basic structure and are not considered tax preferences even though they are subtractions from net income. These include differential rates based on income level, the standard deduction, and personal exemptions. Only exceptions to these basic tax rules can be properly identified as tax preferences.

In defining "tax preference," this Report uses the following operational guidelines found in §8305(6):

> ""Tax preferences' means any law of the United States or of the state of Delaware which exempts, in whole or in part, certain persons, income, goods, services or property from the impact of established taxes, including, but not limited because of a failure of enumeration, to those devices known as tax deductions, tax exclusions, tax credits, tax deferrals, and tax exemptions. Tax preferences shall not include variations in the rate of income tax...standard deductions...or personal exemptions."[2]

There are several types of tax preferences. It is important to understand how each works, because the value of a preference will differ based on the mechanics of its delivery. Types of tax preference include:

- Exemptions
  A tax *exemption* occurs when certain activities or goods, normally subject to taxation, are instead considered free of tax obligations. For example, the business activities of charitable organizations are tax exempt. Some exemptions are not required to be reported. Because of this, it can be difficult to estimate the value of these preferences.

- Exclusions
  A tax *exclusion* occurs when a portion of certain activities or goods, normally subject to taxation, are instead considered free of tax obligations. For example, $12,500 of pension/retirement income is excludable from taxable income for

[2] The personal exemption was replaced by a personal credit effective January 1, 1996.

taxpayers 60 years and older. Pension/retirement income above that amount is subject to the income tax.

- Deductions
  A tax *deduction* reduces the base which is subject to taxation. For example, an income tax deduction will reduce the amount of income which is subject to tax. At a tax rate of 6.6%, a $100 deduction will have a value of $6.60.

- Credits
  A tax *credit* reduces a tax liability dollar-for-dollar. Tax credits may be either refundable or nonrefundable. Nonrefundable tax credits cannot reduce a tax bill below $0, while refundable tax credits can and may potentially result in a negative tax liability.

Review of Tax Preference Terminology

Tax systems are frequently evaluated according to several commonly accepted criteria. Tax preferences affect whether a tax system meets these criteria. Therefore, it is appropriate to assess tax preferences in terms of their effect on the tax system. Criteria used to assess a tax system include:

- Ability to raise revenues in a reliable manner, known as *adequacy and stability*;
- Fairness in terms of the distribution of the tax burden, known as *horizontal equity* (i.e., treating equals equally) and *vertical equity* (treating unequals fairly based on their ability-to-pay);
- Ease of administration, enforcement, and return preparation, known as *simplicity*;
- Amount of interference with individual decision-making, known as *economic efficiency*; and
- Potential to promote (or hinder) *economic growth*.

Adequacy and Stability

Tax preferences impact a tax system by reducing government revenues. They are often referred to as "tax expenditures" to indicate their net negative impact on the government's budget. Producing sufficient revenue, even during economic downturns, is one of the most important roles of any tax system. Tax preferences affect the *adequacy* of tax systems by narrowing the tax base and reducing certain taxpayers' liabilities. This then reduces the ability of a tax system to raise revenue in a *stable* and *reliable* manner through

the peaks and troughs of the economic cycle. Tax preferences linked to certain income sources or investment activities increase revenue instability because taxpayers can change their economic behavior in unpredictable ways.

A related concept, which is often discussed in connection with adequacy, is the *income elasticity* of a particular revenue source. Tax elasticity refers to the percentage change in revenue attributable to a one-percent change in the income of taxpayers. Revenue sources are often assigned an income elasticity value and rated accordingly. For example, an income elasticity of 0.5 would mean that a one-percent change in income would result in a 0.5 percent change in tax revenue.

Elasticity is an important consideration in evaluating tax systems because it is desirable to have revenue sources in place which keep pace with inflation and the demand for public services. In most instances, an income elasticity of at least 1 is desired – this implies that a one percent increase in income will produce a one percent increase in tax revenue. Within a single revenue source, tax stability and sufficient tax income elasticity are often difficult to achieve simultaneously; the more income elastic a revenue source, the less stable and predictable it is likely to be. For this reason, a state's "revenue portfolio" should contain a diverse mix of taxes, creating a proper balance between revenue growth and stability. The DEFAC Advisory Council on Revenues issued a report in May, 2015 suggesting a path towards a more properly balanced "revenue portfolio" for Delaware. For additional information on the tradeoffs between the evaluative criteria discussed in this section, please refer to the summary below.

Horizontal Equity

Horizontal equity means that taxpayers with similar ability-to-pay should have similar net tax burdens. Generally speaking, equal ability-to-pay is defined in terms of equal income, but income does not always equate with ability-to-pay. For example, if "Taxpayer A" and "Taxpayer B" have the same level of income, but Taxpayer A spends two-thirds of her income on unavoidable medical expenses, then Taxpayer A has less ability-to-pay than Taxpayer B. Horizontal equity, therefore, does not necessarily imply one set of rules for all. Tax rules can be adjusted to take account of special circumstances and maintain horizontal equity. The problem is determining *which* special circumstances justify special treatment for tax purposes. These special circumstances are typically unavoidable, catastrophic expenses that a taxpayer faces involuntarily. Large, voluntary, and common expenses are not usually considered in ability-to-pay calculations because of their controllability. When it is legitimate to deviate from a common definition of income, criteria defining these cases should be outlined, and tax preferences evaluated with respect to them.

Vertical Equity

Vertical equity is the principle that tax burdens should be distributed "fairly" among taxpayers with different abilities-to-pay. Tax systems may be progressive, proportional, or regressive. However, vertical equity is a subjective concept that is open to debate. Among policymakers and academics, there is general agreement that the tax system should not be regressive – taxpayers with lower incomes should not pay a larger proportion of their income in taxes than do those with higher incomes. Some tax preferences are clearly intended to benefit low-income groups.

The intent of these preferences, with respect to their effect on tax burdens, is different from horizontal equity. Tax preferences that improve horizontal equity are intended to equalize the tax treatment between individuals with similar incomes by recognizing differences in ability to pay. Typically, tax preferences that seek to address vertical equity are designed to increase the tax system's progressivity by reducing the tax burden on lower-income taxpayers relative to those with higher incomes. To the extent that they are successful, proponents of increased progressivity may claim that the tax preference improves vertical equity. However, several of Delaware's tax preferences provide significant tax benefits to middle- and upper-income taxpayers even though they were ostensibly established for the purpose of improving vertical equity.

Simplicity

Tax system *simplicity* decreases taxpayer and administrative costs and increases compliance with tax laws. Tax preferences may take the form of deductions, exemptions, credits, and exclusions, many of which make tax forms more difficult to understand, more time-consuming, and harder to complete accurately. Entitlement to special deductions often requires special recordkeeping by taxpayers and additional verification by revenue agents. Simple tax systems offer reduced administrative and collection costs due to their transparent, straightforward definition of taxable income.

Simplicity can affect voluntary and involuntary compliance rates. The possibility that taxpayers will make inadvertent mistakes calculating their liability increases with the number of deductions and credits available. Tax simplification can increase voluntary compliance rates. Fewer deductions and credits (which are often difficult to verify without conducting an audit) provide fewer opportunities to shelter income. Reducing the number of tax preferences reassures taxpayers that other citizens are "paying their fair share" and increases their willingness to comply voluntarily.

Economic Efficiency

An efficient tax system should be as neutral as possible with respect to economic decision-making. This requires that resources be allocated where they will receive the highest expected return. Tax preferences may interfere with economic decision making and erode *economic efficiency* because they explicitly favor certain activities over others.

Not only does society lose resources by limiting tax payments from certain taxpayers, but tax preferences also may shift economic resources towards less productive uses. Tax preferences can cause resources to be allocated where they can receive the most favorable tax treatment rather than where they can produce the goods and services most in demand by consumers, or earn the highest economic return. In the worst-case scenario, taxpayers may be able to take advantage of a tax preference without any change to existing activity. In these cases, the tax preference would act more as a "bonus" than an economic incentive.

Economic Growth

Many tax preferences are based on the argument that they will promote economic development by encouraging businesses to locate in Delaware or to invest in existing Delaware enterprises. Tax preferences can increase tax revenues if they attract investments that enlarge the economy. Whether preferences *do* enhance economic growth is questionable. Tax preferences for certain activities may impede growth if they result in higher tax rates for other, non-preferred activities. Higher rates hinder economic growth because they reduce the after-tax return available on investments.

Other Criteria

Tax preferences are often established for reasons other than improving the tax system and should be measured against criteria in addition to those listed above. Many preferences are designed to provide incentives to certain investment activities or to serve specific constituencies. In these cases, the tax system is being used as a mechanism to achieve public policy goals that are unrelated to tax administration. For example, the purpose of some business tax credits is to increase business investment in certain industries, locations, or production methods, such as expenditures on pollution abatement equipment. These external policy goals must be recognized in any assessment of a tax preference. The primary questions in these cases are whether the tax preference actually causes the behavioral change that society desires, and if another mechanism (aside from the Tax Code) is more appropriate in achieving the desired goal.

Summary

One final point to keep in mind is that, in practice, there are tradeoffs between these different criteria. For example, efforts to improve horizontal equity by instituting new tax deductions or credits to insulate taxpayers from unavoidable expenditures may erode simplicity. Tax structures designed to produce a more progressive distribution of tax burdens may violate the principal of economic efficiency. A tax system cannot achieve each of these goals to the same degree simultaneously. Ideally, these fundamental criteria are balanced in a way that reflects the desires of state taxpayers as expressed through their elected representatives.

Readers will likely form more fundamental questions as they read this Report. To list a few:

(i) Should the tax system go beyond its basic role of raising government revenues? If so, what are these roles?

(ii) If the tax code is being used to address a certain societal problem, would direct governmental expenditures or the imposition (or removal) of government regulations better address the problem?

(iii) To what degree should tax preferences be held to the traditional standards of tax administration (i.e., adequacy, equity, efficiency, and simplicity), even if a tax preference was not created for tax policy purposes?

Methodology – Measurement of Revenue Impacts

The revenue impacts of Delaware tax preferences are analyzed using a variety of sources and techniques. Estimates of losses in the personal income tax system rely primarily on databases that include information from state and federal personal income tax forms for individuals filing returns in Delaware. Because Delaware has a relatively small number of taxpayers, in many instances the Division of Revenue can analyze data for all resident and non-resident taxpayers, rather than resort to statistical samples of the population. Modern relational database software packages combine with the relatively small number of Delaware taxpayers to create substantially more accurate measures of specific tax preference impacts on individual income tax revenues.

Other sources of information for this Report include computerized data for corporate income and other tax sources; published and unpublished Department of

Finance reports and fiscal notes; data and reports from other government agencies and private institutions; and, where necessary, direct sampling of Delaware tax returns.

Readers should be aware of several limitations with respect to the Report's fiscal impact calculations:

(i) Except where noted, revenue loss estimates for each tax preference are calculated in static terms without accounting for behavioral effects that may result from the elimination or modification of a specific tax preference. This limitation is most significant with respect to business tax credits whose primary purpose is to encourage behavioral change, such as different patterns of business investment.

(ii) Revenue loss estimates are calculated *separately* for each tax preference. No assessment has been made of the cumulative effect of a number of tax preferences on lost revenues. Interrelationships between different tax preferences can result in situations in which changing one preference has implications for the revenue loss estimates of other preferences. This limitation is most apparent with respect to tax preferences for the elderly. The elderly may claim up to four different, non-means-tested tax preferences. Due to Delaware's graduated rate structure, the revenue effect of claiming four tax breaks simultaneously is not necessarily the same as the sum of its parts. For example, an elderly couple that qualifies for three tax preferences may avoid any tax liability by taking only one of the three preferences available to them.[3]

(iii) Revenue estimates assume no change in the taxpayer's decision to itemize deductions or to take the standard deduction. If several preferred itemized deductions were eliminated, more taxpayers would possibly claim the standard deduction instead. As a result, the revenue impacts of other itemized deductions would fall. Conversely, elimination of the additional standard deduction for the elderly might cause an increase in itemized deductions, which would affect the fiscal impact of other tax preferences.

(iv) The fiscal impact of a particular provision only examines the revenue losses related to a specific tax covered in this Report. This is significant for several of the business tax credits, which may be taken against taxes other than corporate income tax or public utility taxes. For example, while a firm may have no corporate income against which to claim credits, it may claim the credits against the gross receipts tax, which is not covered in this Report.

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[3] See the section of this Report entitled "Incrementalism" below.

(v) Economic performance directly affects these revenue loss estimates, especially those for corporate income tax preferences. For example, in economic downturns, corporations may not have any taxable income due to net losses. Corporations with no liability cannot claim the tax credits to which they may be entitled. As such, estimates of tax expenditures depend on the predictability of changes in taxable income that result from changes in the national economy.

(vi) Changes in the federal tax or regulatory system can also affect the revenue loss estimates for Delaware tax preferences. This is because changes at the federal level may induce behavioral changes that affect the state revenues.

(vii) Both federal and Delaware specific tax return data lags behind the Report's estimation period. As a result, estimates are generated using economic assumptions about fiscal year data that has not yet been finalized.

Despite these limitations, this Report's revenue loss estimates do provide useful information on the relative size and growth of various tax preferences. The estimates can show how widely a tax preference is being used and indicate the revenue implications associated with its repeal or modification.

Limitations of the Tax Preference Report – Incrementalism

This Report examines individual preferences within specific revenue categories. One of the shortcomings of this approach is that, in some instances, it fails to adequately convey the implications which can result from the cumulative effect of multiple tax preferences. The incremental nature with which some preferences develop can have unintended consequences on taxpayers and state revenues. Due to the efforts of state policymakers, Delaware has for the most part avoided this problem. Two areas where incrementalism has raised concerns are the complexity of the New Job Creation Credit (formerly, the "Blue Collar Jobs Act" credits) and personal income tax preferences based on age. The discussion below deals with personal income tax preferences based on age.

Over the past five decades, public policy makers at all levels of government have implemented proposals aimed at improving the welfare of elderly citizens. The creation of Medicare and indexing Social Security benefits are among the most notable federal policies aimed at assisting the elderly. Like other states, Delaware has enacted several personal income tax preferences to assist elderly taxpayers.

Evaluated individually, the unintended implications of these preferences (see the Personal Income Tax section below) may not have sufficiently outweighed the perceived

benefits to prevent their enactment. Taken together, however, serious equity implications can arise. Because elderly taxpayers can utilize more than one of these preferences at a time, the combined effect of these preferences can result in dramatically different tax treatment of individuals with the same ability-to-pay.

Cumulative Effect of Non-means Tested Preferences

An illustration of the equity problems caused by the cumulative effect of these tax preferences can be seen in the following example. Consider the following two households:

	Household A	Household B
Family size:	4	2
Both Spouses Age:	35	65
Number of Children:	2	0
Both Spouses Work:	Yes	No
Total Household Income:	**$74,400**	**$74,400**

"Household A" receives its income exclusively from wages and interest, while "Household B" receives its income primarily from Social Security and pension income. The differences in sources of income between these two households will have a dramatic impact on their tax liability.

Household A

	Spouse 1	Spouse 2
Pension:	$0	$0
Interest:	$500	$500
Dividends:	$0	$0
Wages:	$36,700	$36,700
Social Security:	$0	$0
Total Income:	**$37,200**	**$37,200**

Household B

	Spouse 1	Spouse 2
Pension:	$20,000	$20,000
Interest:	$7,200	$7,200
Dividends:	$0	$0
Wages:	$0	$0
Social Security:	$10,000	$10,000
Total Income:	**$37,200**	**$37,200**

In computing taxable income, each spouse in Household A can reduce its taxable income by $3,250 (a total of $6,500 – the amount of the standard deduction). The couple in Household B, meanwhile, can eliminate taxable income almost completely because of the sources of their income and their age. This reduction represents the exclusion of Social Security benefits, the pension and eligible retirement income exclusion, the low-income elderly exclusion, the standard deduction and the additional standard deduction for persons 65 and over. (See table below.)

Tax Liability Comparison
Two-Earner Family of Four vs. Two Taxpayers Over 65

	Household A		Household B	
Type of Income	Spouse 1	Spouse 2	Spouse 1	Spouse 2
Total Income	$37,200	$37,200	$37,200	$37,200
Wages	$36,700	$36,700	$0	$0
Social Security Exclusion	$0	$0	-$10,000	-$10,000
Pension Income	$0	$0	$20,000	$20,000
Dividend Income	$0	$0	$0	$0
Interest Income	$500	$500	$7,200	$7,200
Total Pension/Retirement Income	$0	$0	$27,200	$27,200
Pension Exclusion	$0	$0	-$12,500	-$12,500
Delaware AGI	$37,200	$37,200	$14,700	$14,700
Standard Deduction	-$3,250	-$3,250	-$3,250	-$3,250
Additional Standard Deduction	$0	$0	-$2,500	-$2,500
Taxable Income	$33,950	$33,950	$8,950	$8,950
Gross Tax Liability	$1,497	$1,497	$220	$220
Personal Credit	-$330	-$110	-$110	-$110
Additional Personal Credit	$0	$0	-$110	-$110
Child Care Credit	$0	-$250	$0	$0
Net Liability	$1,167	$1,137	$0	$0
Total Household Liability	**$2,304**		**$0**	

In the end, Household A has a gross liability of $2,994 which is reduced to $2,304 through the use of four $110 personal credits and the child care credit.[4] Household B, on the other hand, has $440 in gross liability. This liability is completely eliminated because the couple in Household B qualifies for four $110 personal credits – two regular credits and two additional credits for persons age 60 or over. The retirees in Household B pay no income tax despite having the same income and no dependents, while the working family of four owes the state over $2,300.

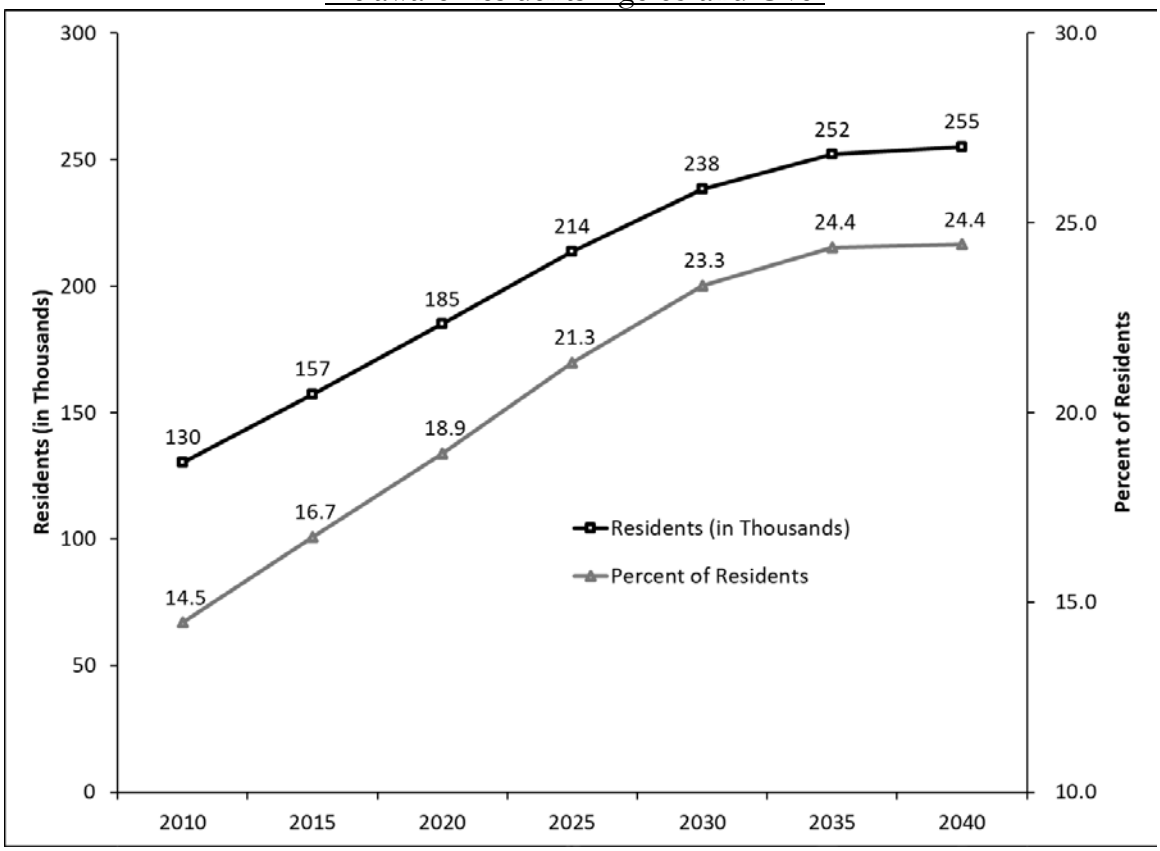
This example is representative of the radically different tax treatment of similarly situated taxpayers possible through the cumulative effect of non-means tested tax preferences.

Long-Term Effect on State Revenues

The cost of these preferences is expected to increase dramatically in future years. From 2010 to 2040, the percentage of the population age 65 and over will increase dramatically as baby-boomers transition into retirement. This will significantly increase the cost of age-based tax preferences as more and more elderly taxpayers become eligible for them. The number of Delaware residents age 65 and over is expected to increase to approximately 255,000 by the year 2040 – *doubling in size* since 2010 (see chart below). The percentage of all Delawareans over age 65 is expected to increase from 14.5 percent in 2010 to 24.4 percent in 2040.

[4] This couple can use four personal credits – one personal credit for each spouse and one for each dependent.

Delaware Residents Age 65 and Over[5]



[5] *Source: Delaware Population Consortium, Annual Population Projections, 2019 (https://stateplanning.delaware.gov/demography/documents/dpc/DPC-2019v0-single-year-5year-age-cohorts.xls)*

LIST OF DELAWARE TAX PREFERENCES

Personal Income Tax

1.01 Low-Income Elderly Exclusion

1.02 Exclusion of Pension and Eligible Retirement Income

1.03 Exclusion of Taxable Social Security Benefits

1.04 Additional Standard Deduction for the Blind or Persons Age 65+

1.05 Charitable Mileage Deduction

1.06 Additional Personal Credit for Persons Age 60+

1.07 Volunteer Firefighter's Tax Credit

1.08 Child and Dependent Care Expense Tax Credit

1.09 Tax Credits for New Business Facilities, New Employees, Qualified Investments, and Clean Energy Technology Device Manufacturing

1.10 Military Action Exemption

1.11 Extension of Filing Deadline for Military Personnel Serving in a Combat Zone

1.12 Exemption for Early Retirement Distributions Used for Education

1.13 Exemption for Trusts Established as "Designated" or "Qualified" Settlement Funds

1.14 Land and Historic Resource Tax Credit

1.15 Historic Preservation Tax Credit

1.16 Earned Income Tax Credit

1.17 Exemption of Out-Of-State Resources During Declared Emergencies

1.18 Vocational Rehabilitation Hiring Credit

1.19 Angel Investor Tax Credit ★

Corporate Income Tax

2.01 Exemption of Investment Holding Companies and Firms Managing Intangible Investments of Mutual Funds

2.02 Deduction of Interest from Affiliated Companies

2.03 Handicapped Accessibility Deduction

2.04 Neighborhood Assistance Credit ★

2.05 Credits for New Employment and Qualified Investments in Business Facilities

2.06 Credits for New Employment and Qualified Investments in Targeted Areas

2.07 Clean Energy Technology Device Manufacturing Credit

2.08 Credits for Development of "Brownfield" Sites

2.09 Research and Development Tax Credit

2.10 Land and Historic Resource Tax Credit

2.11 Historic Preservation Tax Credit ★

2.12 Headquarters Management Corporations

2.13 Asset Management Companies

2.14 Business Finder's Fee Tax Credit

2.15 Veteran's Opportunity Credit

2.16 Exemption of Out-Of-State Resources During Declared Emergencies

2.17 New Economy Jobs Credit ★

2.18 Vocational Rehabilitation Hiring Credit

2.19 Apportionment Elections Preference for Worldwide Headquarters and Telecommunication Companies

2.20 Automatic External Defibrillator Tax Credit ★

Motor Fuel/Special Fuel Tax

3.01 Exemption for Ambulances, Veterans' Group Vehicles, and Volunteer Fire Companies

3.02 Refunds for Certain Non-Road Vehicles

3.03 Exemption for Special Fuels

3.04 Aviation Jet Fuel Exemptions ★

Public Utility Tax

4.01 Exemption for Corporations Reorganizing Under Provisions of the Bankruptcy Code

4.02 Exemption of Electricity Used in Certain Manufacturing Processes

4.03 Refunds for Firms That Qualify for New Business Facilities Credit

4.04 Rate Reduction for Electricity used by Manufacturing Firms, Agribusiness and Food Processing Firms

4.05 Rate Reduction for Gas Used by Manufacturing Firms

4.06 Exemption for Electricity used by Automobile Manufacturing Firms

4.07 Exemption for Gas used by Automobile Manufacturing Firms

4.08 Rate Reduction for the Provision of Cable and Satellite Television Services

4.09 Exemption for Electronic Pager Service

★ *New or recently expanded preference*

DELAWARE TAX PROVISIONS NOT INCLUDED

The following items are listed in the Delaware Code in a manner similar to other tax preferences detailed in this Report. Many of the items meet the criteria used to define a tax preference as highlighted above. However, these tax preferences have been excluded from the Report for the reasons noted below.

Personal Income Tax

1. Modification for Fiduciary Adjustment
   Title 30, Delaware Code, Chapter 11, §1106(c).

   Rationale for exclusion from Report:
   This modification is viewed as an appropriate adjustment to determine net income and, as such, should not strictly be defined as a tax preference.

2. Deduction of Interest or Dividends on U.S. Government Obligations
   Title 30, Delaware Code, Chapter 11, §1106(b)(1).

   Rationale for exclusion from Report:
   This modification is required by the Supremacy Clause of the U.S. Constitution.

3. Deduction for Wages Paid for Which New Jobs Tax Credit is Claimed
   Title 30, Delaware Code, Chapter 11, §1106(b)(5).

   Rationale for exclusion from Report:
   This provision is not technically a tax preference because a deduction is allowed for all wages paid, even when the taxpayer elects the federal preference of taking a credit for the same wages.

4. Credit for Income Taxes Paid to Another State
   Title 30, Delaware Code, Chapter 11, §1111.

   Rationale for exclusion from Report:
   This credit avoids double taxation of Delaware residents. Further, the Supreme Court ruled in *Wynne v. The Comptroller of the State of Maryland* that the Dormant Due Process Clause requires this credit to exist.

5. Favorable Tax Treatment of Distributions from Qualified Tuition Savings Plans
   Title 14, Delaware Code, §3483.

   Rationale for exclusion from Report:
   This is a preference authorized under the federal Internal Revenue Code (IRC). State taxpayers benefit by virtue of Delaware's "piggybacking" on the federal tax system.

6. Deduction of Health Insurance Costs Paid by Self-Employed Persons
   Title 30, Delaware Code, Chapter 11, §1109(a)(2)(b)

   Rationale for exclusion from Report:
   This preference allows a state income tax deduction for amounts spent on health insurance over and above that which is allowed as a deduction on the taxpayer's federal return. Beginning in Tax Year 2003, the federal exclusion increased to 100% of qualified expenses and effectively eliminated any benefit associated with Delaware's "preference."

Corporate Income Tax

1. Deduction for Interest Received from U.S. Government Securities
   Title 30, Delaware Code, Chapter 19, §1903(a)(1).

   Rationale for exclusion from Report:
   This deduction is required by Constitutional provision.

2. Deductions for Gains or Losses From Sale of U.S. Government Securities
   Title 30, Delaware Code, Chapter 19, §1903(a)(2)(c).

   Rationale for exclusion from Report:
   These deductions are required by Constitutional provision.

3. Deduction for Wages Paid for Which New Jobs Tax Credit is Claimed
Title 30, Delaware Code, Chapter 19, §1903(a)(2)(e).

Rationale for exclusion from Report:
As with the personal income tax exemption, this provision is not technically a tax preference because a deduction is allowed for all wages paid, even when the taxpayer elects the federal preference of taking a credit for the same wages.

4. Exemption of Foreign Interest, Dividends, and Royalties
Title 30, Delaware Code, Chapter 19, §1903(a)(2)(a).

Rationale for exclusion from Report:
These sources are not included due to Constitutional limitations.

5. Exemption for Homeowners' Associations
Title 30, Delaware Code, Chapter 19, § 1902(b)(14).

Rationale for exclusion from Report:
These entities are not considered part of the base of the tax, and therefore the exemption is not defined as a tax preference.

Motor Fuel/Special Fuel Tax

1. Motor Fuel Tax and Special Rates
Title 30, Delaware Code, Chapter 51, §5110(c), §5132.

Rationale for exclusion from Report:
This provision is not regarded as a tax preference because different tax rates are applied to technically different tax bases.

2. Exemption for Sales of Gasoline to the U.S. Government or Any of Its Subdivisions
Title 30, Delaware Code, Chapter 51, §5111(a)(1).

Rationale for exclusion from Report:
This exemption is required by Constitutional provision.

3. Exemption for Sales of Gasoline to Anyone Protected by the Interstate Commerce Clause
   Title 30, Delaware Code, Chapter 51, §5111(a)(2).

   Rationale for exclusion from Report:
   This exemption is required by Constitutional provision.

4. Exemption for Sales of Gasoline to Delaware or Any of Its Subdivisions
   Title 30, Delaware Code, Chapter 51, §5111(a)(5).

   Rationale for exclusion from Report:
   This exemption avoids the state needlessly taxing itself.

5. Exemption for Sales of Special Fuels to the U.S. Government or Any of Its Subdivisions
   Title 30, Delaware Code, Chapter 51, §5133(a)(1).

   Rationale for exclusion from Report:
   This exemption is required by Constitutional provision.

6. Exemption for Sales of Special Fuels to Delaware or Any of Its Subdivisions
   Title 30, Delaware Code, Chapter 51, §5133(a)(2).

   Rationale for exclusion from Report:
   This exemption avoids the state needlessly taxing itself.

7. Exemption of Fuel Used and All Vehicles of Any Other State Government Which Reciprocates
   Title 30, Delaware Code, Chapter 51, §5133.

   Rationale for exclusion from Report:
   This exemption is required by Constitutional provision.

8. Exemption for Sales of Aviation Jet Fuel to the U.S. Government or Any of Its Subdivisions
   Title 30, Delaware Code, Chapter 51, §5172(b)(1).

   Rationale for exclusion from Report:
   This exemption is required by Constitutional provision.

9. Exemption for Sales of Aviation Jet Fuel to Delaware or Any of Its Subdivisions
Title 30, Delaware Code, Chapter 51, §5172(b)(2).

Rationale for exclusion from Report:
This exemption avoids the state needlessly taxing itself.

Public Utility Tax

1. Exemption for Electricity, Gas and Telephone Sales and Services to Residential Users
Title 30, Delaware Code, Chapter 55, §5506(e).

Rationale for exclusion from Report:
These users are not considered part of the base of the tax, and therefore the exemption is not defined as a tax preference.

2. Exempt Tax Receipts Received From the Sale of Public Utilities to the State of Delaware or Any of Its Subdivisions
Title 30, Delaware Code, Chapter 55, §5506(d).

Rationale for exclusion from Report:
This exemption avoids the state needlessly taxing itself.

3. Exempt Internet Access Charges from Public Utility Tax
Title 30, Delaware Code, Chapter 55, § 5502

Rationale for exclusion from Report:
This preference is effectively authorized under Delaware's own Tax Code. Authorization of this exemption became effective for Delaware taxpayers on January 1, 2005. As of November 1, 2005, however, an update to federal law effectively replicated Delaware's provision thereby eliminating any benefit associated with Delaware's "preference."

A SUMMARY OF TAX PREFERENCE CHANGES SINCE 2017

Since the last Tax Preference Report was issued in 2017, Delaware has created three new tax preferences and expanded three existing tax preferences. Below is a summary of the legislative changes affecting tax preferences since the completion of the 2017 Report.

Tax Preferences Created

Personal Income Tax:

- Angel Investor Tax Credit

Corporate Income Tax:

- Automatic External Defibrillator Tax Credit

Motor Fuel/Special Fuel Tax

- Aviation Jet Fuel Exemptions

Tax Preferences Expanded

Corporate Income Tax:

- Historic Preservation
  Increased the maximum amount awarded to $8 million.

- Neighborhood Assistance
  Increased the maximum amount awarded to $1 million.

- New Economy Jobs Credit
  Allowed employers to pro-rate their job creation activity in the first certified year and updated the salary threshold index.

PERSONAL INCOME TAX

- Statutory Provision

  Title 30, Delaware Code, Chapter 11.

- Collection/Administrative Agency

  The Department of Finance, Division of Revenue, administers this tax.

- General Liability

  Resident

  Every resident of Delaware must file a personal income tax return whenever such resident:

  (a) Is required to file a federal tax return; or

  (b) Has adjusted gross income (after modifications) that exceeds the maximum filing thresholds. The maximum filing thresholds for each filing status are listed below:

AGE/STATUS	FILING SINGLE	MARRIED FILING A JOINT RETURN (1)	MARRIED FILING SEPARATE	FILING AS A DEPENDENT ON ANOTHER PERSON'S RETURN
Under 60	$9,400	$15,450	$9,400	$5,250
60 to 64	$12,200	$17,950	$12,200	$5,250
65 and over OR Blind	$14,700	$20,450	$14,700	$7,750
65 and over AND Blind	$17,200	$22,950	$17,200	$10,250

(1) This dollar amount represents a taxpayer's individual Adjusted Gross Income, NOT a total combined with anyone else.

Every resident must report all income earned during the taxable year to Delaware, regardless of the source.

Nonresident

Every nonresident must file a tax return to report all income earned within the state. This includes only income attributable to employment or personal services performed in Delaware, or to the ownership or disposition of any interest in real or tangible personal property in Delaware (i.e., wages, business income, capital, rents and royalties, partnerships, farm income and any other income derived from a Delaware source). Interest, dividends and pensions, even if attributable to Delaware employment, are excluded.

Nonresidents calculate their liabilities as if they were residents except that nonresidents' final liabilities are prorated according to their ratio of Delaware source income to total income.

Part-Year Resident

Part-year residents have the option of filing as a resident or a nonresident. By filing as a nonresident, final liability is reduced because it is prorated according to the taxpayer's ratio of Delaware source income to total income. Filing a resident return allows the taxpayer to make use of certain tax credits, such as the child care credit, that are not available to nonresidents. If large enough, these tax credits can produce a final liability that is lower than that which may be obtained by filing as a nonresident.

- Tax Rates

For Tax Years 2014 and after, taxable income is assessed at the following rates:

If Taxable Income is Greater Than:	But Less Than:	Tax Liability is Calculated As:	Plus:	On Taxable Income Over:
$0	$2,000	$0.00	0.00%	$0
$2,000	$5,000	$0.00	2.20%	$2,000
$5,000	$10,000	$66.00	3.90%	$5,000
$10,000	$20,000	$261.50	4.80%	$10,000
$20,000	$25,000	$741.50	5.20%	$20,000
$25,000	$60,000	$1,001.00	5.55%	$25,000
$60,000		$2,943.50	6.60%	$60,000

- Tax Receipts, net of refunds (millions of dollars)

Fiscal Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total ($)	853.1	997.2	1,041.9	1,139.8	1,187.7	1,251.9	1,286.6	1,333.2	1,428.2	1,527.5

- Tax Preferences

The following table identifies personal income tax preferences within the Delaware Code along with annual estimated costs. Links within the table navigate to more detailed analysis of each tax preference.

TAX PREFERENCE	FY 19 (EST)	FY 20 (EST)
1.01 Low-Income Elderly Exclusion	Negligible	Negligible
1.02 Exclusion of Pension and Eligible Retirement Income	$65.5 - $69.9m	$68.5 - $73.0m
1.03 Exclusion of Taxable Social Security Benefits	$73.3m	$79.4m
1.04 Additional Standard Deduction for the Blind or Persons Age 65 or Over	$6.0m	$6.4m
1.05 Charitable Mileage Deduction	Negligible	Negligible
1.06 Additional Personal Credit for Persons Age 60 and Over	$14.1m	$14.8m
1.07 Volunteer Firefighter's Tax Credit	$1.7m	$1.8m
1.08 Child and Dependent Care Expense Tax Credit	$5.9m	$6.1m
1.09 Tax Credits for New Business Facilities, New Employees, Qualified Investments, and Clean Energy Technology Device Manufacturing	$550,000	$500,000-$700,000
1.10 Military Action Exemption	Negligible	Negligible
1.11 Extension of Filing Deadline for Military Personnel Serving in a Combat Zone	Negligible	Negligible
1.12 Exemption for Early Retirement Distributions Used for Education	$2.4 - $3.2m	$2.6 - $3.4m
1.13 Exemption for Trusts Established as "Designated" or "Qualified" Settlement Funds	Unknown	Unknown
1.14 Land and Historic Resource Tax Credit	(D)	(D)
1.15 Historic Preservation Tax Credit	$925,000	$1.5 - $1.7m
1.16 Earned Income Tax Credit	$12.5m	$13.6m
1.17 Exemption of Out-Of-State Resources During Declared Emergencies	Negligible	Negligible
1.18 Vocational Rehabilitation Hiring Credit	$0	Negligible
1.19 Angel Investor Tax Credit	N/A	(D)

(D) = Per 30 Del. C. §368, the Department of Finance is prohibited from disclosing tax return information identifying specific taxpayers.

1.01 Low-Income Elderly Exclusion

1. Statutory Provision
   Title 30, Delaware Code, Chapter 11, §1106(b)(2).

2. Description
   The law provides for exclusions from gross income to persons who meet certain qualifications. If a taxpayer is single, or married and filing separately, the law allows an exclusion of $2,000 to any person:

   (a) Who is totally and permanently disabled, or who is 60 years of age or older;
   (a) Whose earned income for the year is less than $2,500; and,
   (b) Whose Delaware adjusted gross income (before this deduction) does not exceed $10,000.

   A husband and wife filing a joint return are entitled to an exclusion of $4,000 if the following conditions are met:

   (a) Each is at least 60 years of age, or totally and permanently disabled;
   (b) Their total earned income in the taxable year is less than $5,000; and
   (c) Their Delaware adjusted gross income (without reduction of this exclusion) does not exceed $20,000.

3. Estimated Revenue Loss
   FY 19: Negligible[1]
   FY 20: Negligible

4. Assessment
   The purpose of this provision is to allow elderly or disabled taxpayers with low income to exclude a portion of their income from taxes. Because certain forms of income are not included in this means test, some higher-income elderly taxpayers may qualify for this preference. Conversely, elderly taxpayers who rely primarily on wage income may not qualify for this exclusion even though they otherwise meet the definition of "low-income."

[1] Defined as less than $50,000.

5. Inadvertent Effects

This provision suffers from a number of defects, which at the time of its original enactment appear to have been overlooked. As the size and scope of other tax preferences expanded, these defects became more prominent.

The eligibility means test is poorly designed, resulting in an application of tax relief that follows no rational pattern. Though ostensibly targeted to help "low-income" elderly taxpayers, in practice, this provision was nearly as likely to help middle- and high-income taxpayers as it was to help the poor. For example, the fact that the income of a taxpayer's spouse is not taken into consideration in determining eligibility means that well-to-do couples may enjoy a "low-income" tax preference simply because their income is unequally distributed between spouses. Some low-income elderly taxpayers were denied relief (elderly wage earners, for example) simply because the composition of their income did not conform to the statute's requirements. Finally, the deduction was "all or nothing." If taxpayers meet the means test, the full deduction is awarded. If taxpayers exceeded the means test amount by one penny, they received nothing.

For taxpayers age 60 and over, events have rendered this tax preference practically useless. Other elderly tax preferences have expanded to such an extent that, beginning in tax year 2000, all taxpayers meeting this provision's eligibility requirement and using the standard deduction already have no tax liability.

Taxpayers who choose to itemize their deductions may still benefit from this provision, provided their itemized deductions are less than the standard deduction amount. Low-income taxpayers who would choose to do so are rare and are most likely the spouse of a high-income taxpayer who makes use of most of the couple's itemized deductions. Because this provision's intended beneficiaries are age 60 and over and already have no tax liability, policymakers should seriously consider its elimination or limit its application to disabled taxpayers.

Modifying the provision's means test to be more inclusive would merely result in the extension of tax relief to middle- and upper-income elderly taxpayers. If policymakers desire such a result, it could be more efficiently achieved through simpler and more targeted means.

1.02 Exclusion of Pension and Eligible Retirement Income

1. Statutory Provision
   Title 30, Delaware Code, Chapter 11, §1106(b)(3).

2. Description
   Certain amounts of income received as pensions from employers or meeting the definition of "eligible retirement income" are excludable from Delaware taxable income. This exclusion is limited to $12,500 a year for taxpayers 60 years and older.

   As defined in §1106(b)(3)b.2(B) of Title 30, eligible retirement income includes:

   - Distributions from qualified retirement plans defined under §4974 of the Internal Revenue Code (IRC);
   - Distributions from cash or deferred arrangements described in §401(k) of the IRC;
   - Distributions from government deferred compensation plans described in §457 of the IRC;
   - Dividends;
   - Capital gains;
   - Interest; and
   - Net rental income

   Taxpayers under 60 years of age may exclude up to $2,000 of pension income per year. These taxpayers may not exclude eligible retirement income.

3. Estimated Revenue Loss[2]
   FY 19: $65.5 – $69.9 million
   FY 20: $68.5 – $73.0 million

4. Assessment
   Unlike the low-income elderly exclusion, the pension exclusion is not means-tested. Any taxpayer with pension or eligible retirement income is entitled to claim this tax preference, regardless of his or her ability-to-pay. The purpose of this provision is to provide a tax reduction to recipients of pension or eligible retirement income; it clearly serves only the intended group.

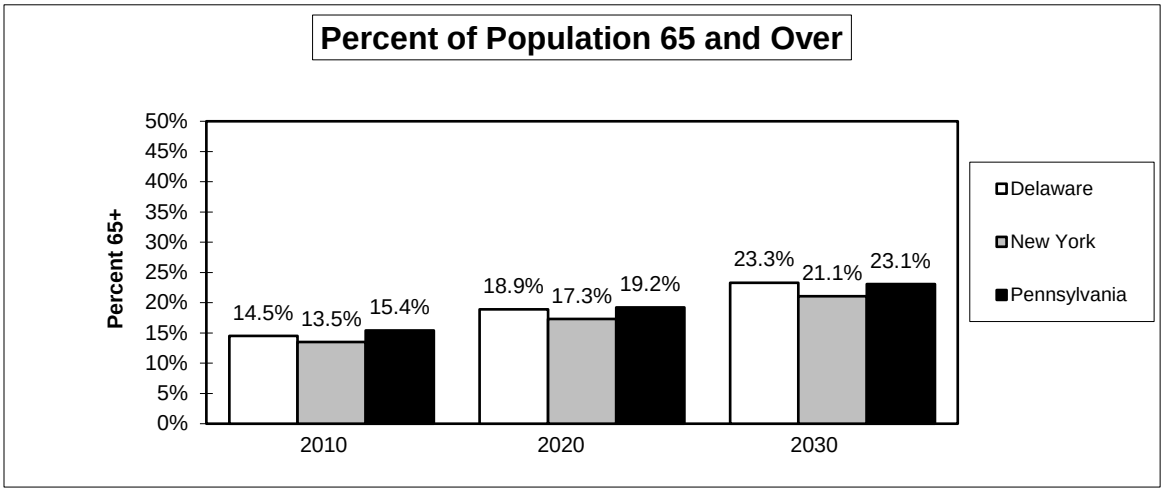
[2] The methodology for estimating the revenue loss from the pension and eligible retirement income exclusion has changed since the last report in 2017 to better account for the proration of non-residents claiming the exclusion.

5. Inadvertent Effects

Delaware's progressive income tax rate structure implies that any non-means-tested, lump-sum exclusion from taxable income – such as the pension and eligible retirement income exclusion – provides a larger tax benefit to higher-income taxpayers than to lower-income taxpayers. For example, "Pensioner A" has $112,500 in income, $100,000 in taxable income once the exclusion is taken. This exclusion will provide Pensioner A with an $825 reduction in tax liability in tax year 2018 ($12,500 x 6.60%). "Pensioner B" has $20,000 in income, $7,500 in taxable income once the exclusion is taken. Because Pensioner B is subject to a lower marginal tax rate, the same $12,500 exclusion will reduce Pensioner B's tax liability by only $578 in tax year 2018 ($10,000 x .048 + $2,500 x.039); significantly less benefit than for the high-income Pensioner A.

With respect to other states in the region, Delaware's maximum pension exclusion of $12,500 may appear to be relatively small. New York allows a maximum pension exclusion of $20,000 and complete exclusion for federal, state, and military pensions.[3] Pennsylvania provides complete exclusion for public and private pension benefits.[4] Some observers argue that elderly taxpayers will migrate to states such as New York and Pennsylvania in order to benefit from their favorable tax treatment of retirement income. There is some anecdotal evidence to support this claim. However, demographic data suggest that it is not a major phenomenon. Academic demography offices in Pennsylvania and New York estimate that the percent of residents over 65 will rise from 15.4% and 13.5% in 2010 to 23.1% and 21.1% by 2030, respectively. The percent of Delawareans over 65 is expected to increase similarly during the same time period: from 14.5% to 23.3%. (See chart below.)

[3] New York Statutes - Article 22, §612(c)(3-a)
[4] Pennsylvania Statutes - Article III, §7301(d)(iii)



Source: The Center for Rural Pennsylvania
(http://www.rural.palegislature.us/documents/reports/Population_Projections_Report.pdf)
Cornell Program on Applied Demographics (https://pad.human.cornell.edu/counties/projections.cfm)
Delaware Population Consortium (https://stateplanning.delaware.gov/demography/dpc-projection-data.shtml)

This suggests that factors other than the tax treatment of retirement income have a more profound impact of the location decisions of retirees. Another real possibility is that the combined impact of Delaware's many retirement tax preferences are, in fact, very competitive relative to other states in the region. Delaware has distinct advantages over neighboring states with respect to property and sales taxes. For the majority of retirees, Delaware's overall tax burden is lower than that of surrounding states.

Proponents of tax preferences for the elderly argue that an increased elderly concentration provides an economic stimulus, especially with respect to service markets. Unless tax preferences for the elderly are significant enough to generate a net increase in tax revenues, then the direct revenue losses imply that marginal tax rates have to be higher than they would be without the preferences in order to generate the same revenues. The effect of elderly preferences, therefore, may be to reduce taxes for taxpayers over age 60 at the cost of increasing taxes for wage earners (whose labor supply decisions are most responsive to changes in after tax wages). Proponents also argue that tax relief based on age is justified because these taxpayers have, after a lifetime of tax paying, paid their "fair share" and at some point deserve relief.

Critics of tax preferences based solely on age disagree with these points for several reasons. Due to the growth in benefit payments and longevity after retirement, many government programs for the elderly are paying significantly more to beneficiaries than the recipients ever paid into the system in taxes.

Estimates show, for example, that most current Social Security recipients will receive many times more in benefits than they and their employers paid into the Social Security system. Because elderly services have grown in cost and total quantity, it takes longer for a person to pay a "fair share" than it did 30 years ago. Another concern is that some exclusions may be taken by persons still in the workforce. This pension exclusion, for example, allows workers who begin to draw a pension at age 45 to exclude $2,000 of income from taxation while other similarly situated taxpayers get no such break.

Finally, preferences that depend only on age or income source are not as closely linked to ability-to-pay as they were at their inception, when persons over age 60 were the poorest segment of society (see discussion below). All elderly preferences, except the low-income exclusion, can be used to reduce liability for even the wealthiest taxpayers as long as they meet the age requirement.

While the extension of eligibility to other sources of retirement income has improved the horizontal equity problems of this preference *among taxpayers over 60*, there are still some equity concerns. [5] When compared to income or other ability to pay considerations, age is a fairly arbitrary criterion for a tax preference. It could be argued that the horizontal equity problems of this preference between taxpayers over and under 60 years of age have been aggravated by this most recent change. For example, consider two hypothetical taxpayers with $1,000 in pension income and $3,500 in other eligible retirement income. "Taxpayer A" is 59 years old, while "Taxpayer B" is 61. Assuming both taxpayers have the same ability to pay, Taxpayer A can only exclude $1,000 while taxpayer B can exclude $4,500. Not only is taxpayer A's exclusion capped at $2,000 in the aggregate, it is limited to traditional pension income. For taxpayers under 60 without pension income, no exclusion is allowed.

As the following table shows, the rate of poverty among the elderly is now lower than the general population. In 1970, 24.6% of those age 65 and over lived under the federal poverty level. By 2018, the proportion had dropped to 9.7%.

[5] The exclusion of pension income alone resulted in more favorable tax treatment for taxpayers whose income is derived from a pension, rather than other forms of retirement income.

Percent of Population Below Federal Poverty Level 2018

Under 18	16.2%
18-24	15.0%
25-34	10.9%
35-44	10.1%
45-54	8.4%
55-59	9.7%
60-64	10.8%
65+	9.7%
Overall Rate	**11.8%**

Source: U.S. Census Bureau, Current Population Survey, 2018 Annual Social and Economic Supplement. https://www.census.gov/data/tables/time-series/demo/income-poverty/cps-pov/pov-01.2018.html

The rate of poverty is significantly lower for the elderly than for children and young adults. As the elderly are statistically less poor than the population as a whole, this age test may benefit taxpayers who do not need relief under any legitimate interpretation of ability-to-pay.

Elderly wage earners who must continue to work to make ends meet are ignored by this provision. Because wages are not eligible for the exclusion, the working poor elderly receive no assistance.

While there is certainly a significant proportion of the elderly population with income below federal poverty levels, policymakers might consider whether government support should more properly continue to be based on age rather than on need and/or ability-to-pay.

1.03 Exclusion of Taxable Social Security Benefits

1. Statutory Provision
   Title 30, Delaware Code, Chapter 11, §1106(b)(4).

2. Description
   The state of Delaware excludes Social Security and Railroad Retirement Board income from the personal income tax. For purposes of federal income taxation, recipients of these benefits who have modified adjusted gross income from all sources above a "base amount" of $25,000 ($32,000 for taxpayers who file jointly) are taxed on a portion of their payments. This taxable portion is the lesser of 50% of the Social Security benefits received, or

50% of a taxpayer's "combined" income over the "base amount." Combined income is 50% of these benefits plus adjusted gross income plus any tax-exempt income or income earned from a foreign country or U.S. possession which is excluded from federal gross income. If a taxpayer's income exceeds $34,000 ($44,000 if married, filing jointly), the lesser of 85% of Social Security benefits or 50% of the combined income above the base amount is included in federal adjusted gross income.

(A complete description of the federal tax code provision relating to social security can be found in IRS Publication 915: Social Security and Equivalent Railroad Retirement Benefits.)

3. Estimated Revenue Loss
FY 19: $73.3 million
FY 20: $79.4 million

4. Assessment
The purpose of this provision is to provide a tax reduction to Social Security and Railroad Retirement Board benefit recipients. This exclusion benefits its intended beneficiaries.

5. Inadvertent Effects
Like the exclusion for certain forms of pension income (Item 1.02), this provision is not a means-tested tax preference. Higher-income taxpayers are eligible for, and benefit more from, this provision than do lower-income taxpayers. As a result, much of the preceding discussion of the pension exclusion is also valid with respect to this exclusion of federal benefits. Despite the fact that this tax relief is provided to Social Security and Railroad Retirement Board recipients because they are perceived as being in need, taxpayers who do not fit this generally accepted perception of being in need may also receive benefits.

Delaware's exclusion of federally taxable Social Security and Railroad Retirement Board benefits effectively removes a federal means test which is designed to limit the preferential tax treatment of such income to those most in need. This vertical equity concern is exacerbated by federal policy which stops the payroll tax at very high wages ($132,900 in 2019). Federally, this means-test counters some of the regressive character of the payroll tax. Only taxpayers over certain income thresholds are required to include such benefits in federal gross income. By definition, only taxpayers who have income above these relatively high thresholds benefit from the exclusion of federally taxable

Social Security or Railroad Retirement Board benefits and the cap on the payroll tax.

1.04 Additional Standard Deduction for the Blind or Persons Age 65 or Over

1. Statutory Provision
   Title 30, Delaware Code, Chapter 11, §1108(b).

2. Description
   Taxpayers who are at least 65 years of age (or blind), and who do not itemize their deductions, are entitled to an additional standard deduction of $2,500. Non-itemizers who are at least age 65 *and also* blind may claim an additional standard deduction of $5,000.

3. Estimated Revenue Loss
   FY 19: $6.0 million
   FY 20: $6.4 million

4. Assessment
   The purpose of this provision is to provide a tax reduction to persons who are blind and/or at least 65 years old. The provision's benefits reach only those for whom it was intended.

5. Inadvertent Effects
   As is the case with the exclusion of pension income (see Item 1.02 above) and the exclusion of taxable Social Security income (see Item 1.03 above), this provision is not means-tested. With respect to this preference's age criterion, many of the same issues that arise with other non-means-tested preferences for the elderly arise here as well. The additional standard deduction benefits many higher-income taxpayers who have no need for tax relief on ability-to-pay grounds but who qualify solely because of their age.

   By definition, an additional standard deduction is not available to taxpayers that itemize their deductions. Because taxpayers that take the standard deduction typically have lower incomes, it may be argued that this additional standard deduction primarily benefits lower-income taxpayers. However, many taxpayers in this age group no longer have mortgage interest deductions, making them less likely to itemize even if they are middle or high-income taxpayers.

An additional standard deduction that is available to individuals who are blind but not to individuals with other disabilities may violate horizontal equity. Taxpayers may have disabilities that affect their ability-to-pay similarly or more severely than blindness, but they would not be eligible for this deduction.

1.05 Charitable Mileage Deduction

1. Statutory Provision
   Title 30, Delaware Code, Chapter 11, §1109(a)(2)(a).

2. Description
   Federal law permits a person who uses his/her automobile to perform voluntary service for a charitable organization to claim an itemized deduction for a portion of those expenses. Under Delaware law, this additional itemized deduction is calculated by subtracting the permissible federal rate for automobile mileage for charitable use (currently 14 cents per mile) from the amount state employees may claim for work-related use of their vehicles (40 cents effective July 1, 2006), or 26 cents per mile.

3. Estimated Revenue Loss
   FY 19: Negligible
   FY 20: Negligible

4. Assessment
   Though small, this preference does provide relief to those individuals who have to drive in order perform voluntary services for charitable organizations. The benefits of this provision go to those intended and do not produce a large fiscal loss. As an itemized deduction, however, the provision does not benefit those taxpayers who use their vehicles for charitable purposes but who take the standard deduction.

   Another concern arises from the fact that only one type of charitable activity (driving) is singled out for favorable tax treatment.

5. Inadvertent Effects
   None noted.

1.06 Additional Personal Credit for Persons Age 60 and Over

1. Statutory Provision
   Title 30, Delaware Code, Chapter 11, §1110(b)(2).

2. Description
Taxpayers who are age 60 and over are entitled to claim an additional non-refundable personal credit. Married taxpayers who file jointly receive an additional $110 credit if only one of the couple is age 60 or older, and an additional $220 if the both persons meet this age test.

3. Estimated Revenue Loss
FY 19: $14.1 million
FY 20: $14.8 million

4. Assessment
The purpose of this provision is to reduce tax liability for persons age 60 and over. Only persons who meet this age test can receive this extra credit, thus ensuring that the provision serves only the intended beneficiaries.

The switch from an extra personal exemption, to an extra non-refundable personal credit for persons over 60 eliminated the regressivity inherent in the additional personal exemption. The value of the tax credit (which reduces tax liability dollar for dollar) is the same for taxpayers in all income ranges.

5. Inadvertent Effects
As discussed above (see items 1.02 and 1.06), age may be an arbitrary condition for grant favorable tax treatment. This preference suffers from the same drawbacks as other non-means-tested tax breaks for the elderly: taxpayers with the same ability-to-pay receive different tax treatment based solely on age, violating horizontal equity.

Moreover, high-income elderly taxpayers receive benefits that are not available to younger taxpayers with substantially less ability to pay, increasing regressivity in the tax code.

1.07 Credit for Expenses Incurred by Active Volunteer Firefighters, Fire Company Auxiliary Members or Members of Volunteer Ambulance or Rescue Service

1. Statutory Provision
Title 30, Delaware Code, Chapter 11, §1113.

2. Description
The provision allows Delaware residents who are active emergency service volunteers to claim a $400 credit against their income tax otherwise due. In order to qualify for the credit, a person must be:
(i) an active volunteer firefighter on call to fight fires on a regular basis; and,
(ii) a voting member of a Delaware volunteer company; or,
(iii) a voting member of a Delaware fire company auxiliary; or,
(iv) an active member of a Delaware volunteer ambulance or rescue service.

3. Estimated Revenue Loss
FY 19: $1.7 million
FY 20: $1.8 million

4. Assessment
The purpose of this credit is to help defray the costs incurred by emergency service volunteers in performing their duties. This is clearly a worthy goal, but it is worth assessing whether it is most appropriately addressed through the tax code. As an alternative, the state could make additional direct annual grants to volunteer fire companies for volunteers' expenses equal to the estimated revenue loss that this preference creates. This approach would avoid an additional complication of the tax code and would simplify administration as the state could work with a manageable number of fire companies rather than reviewing claims by thousands of volunteer firefighters on their tax returns.

5. Inadvertent Effects
None noted.

1.08 Child Care and Dependent Care Expense Credit

1. Statutory Provision
IRC, §21.
Title 30, Delaware Code, Chapter 11, §1114.
2. Description
This non-refundable credit is equal to 50 percent of the federal child and dependent care credit allowed for a given taxpayer. The federal credit amount is determined by applying a percentage (between 20% and 35% depending on the size of adjusted gross income) to qualifying expenses (a maximum of $3,000 for one child, or $6,000 for two or more children). For taxpayers with

federal adjusted gross incomes over $43,000, the maximum credit is 20 percent of qualifying expenses.

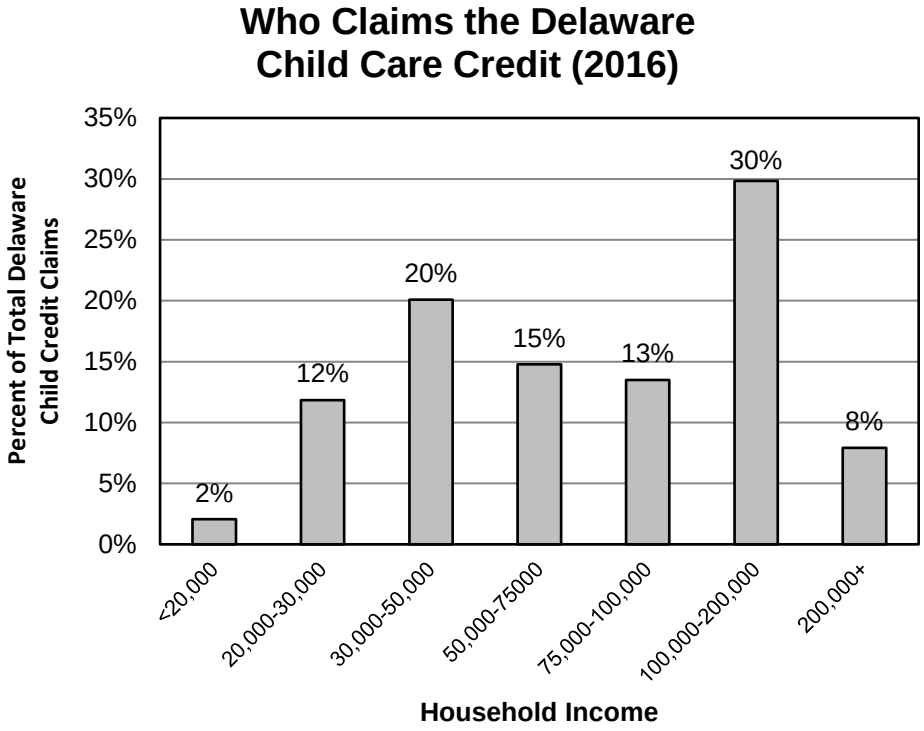
Married couples filing joint federal but separate Delaware returns are limited to applying the credit to the tax liability of the spouse with the smaller taxable income. The credit can be taken for payments made to a relative for child care, provided that the relative is not claimed as dependent on the taxpayer's return and is not the taxpayer's child under the age of 19.

3. Estimated Revenue Loss
FY 19: $5.9 million
FY 20: $6.1 million

4. Assessment
This credit is intended to encourage the expansion of the state's workforce, particularly for entry-level positions, by removing a major obstacle to employment for many potential workers. A significant number of job seekers are single parents in search of relatively low-wage jobs.[6] For these individuals, the high cost of child care is not affordable on the potential wages. The credit, therefore, is intended to offset a significant barrier to entry into the labor force. The degree to which an annual tax subsidy – often received in the form of a refund – is likely to make lower wage jobs economically feasible for parents entering the labor market is debatable.

Although this preference is intended to target economically disadvantaged families, a substantial portion of its benefits accrue to families with moderate and more abundant means. In 2016 roughly 38 percent of the child care credits claimed by Delaware families were claimed by families with Delaware Adjusted Gross Incomes of more than $100,000 (see chart below).

[6] The IRC also allows the credit to be claimed for other persons (e.g., a spouse or parent) who are physically or mentally unable to take care of themselves and claimed as a dependent on the taxpayer's return.



A credit for child care expenses can be viewed as consistent with a definition of taxable income that excludes costs associated with earning income.[7] As such, some observers may not regard the provision as a tax preference. However, some costs of earning income, such as work apparel and commuting expenses, are not deductible. If child care expenses were to be considered non-preferential as a cost of earning income, then this provision should be structured as a deduction from taxable income and not as a credit.

5. Inadvertent Effects
None noted.

1.09 Tax Credits for Creation of Employment, Qualified Investments in Business Facilities, and Clean Energy Technology Device Manufacturing

1. Statutory Provision
Title 30, Delaware Code, Chapter 20, §§2010 - 2040.

[7] This line of reasoning is used to justify a host of deductions against both personal and corporate income taxes for costs incurred in the earning process (e.g., the federal deduction for home office expenses, the federal deduction for business meals).

2. Description
The law offers tax credits for any eligible taxpayer who is not subject to the corporate income tax under the same terms as those discussed below for items 2.05, 2.06, and 2.08. Resident shareholders in eligible S Corporations are entitled to a proportionate share (based on the percentage of ownership in the organization by the taxpayer) of the credits listed. The credits are limited to 50% percent of the tax owed multiplied by the taxpayer's share of distributable income of the S Corporation.

3. Estimated Revenue Loss
FY 19: $550,000
FY 20: $500,000 - $700,000

4. Assessment
This provision extends the credits available under the corporate income tax and gross receipts tax to those eligible taxpayers who are subject to the personal income tax—S corporation shareholders and owners of other pass-through entities. These personal income tax credits raise the same issues as the investment tax credits discussed later in this Report's corporate income tax section. For example, the credits may be too small to generate a significant incentive to increase investments in the intended industries and locations. Many businesses and individuals may be receiving tax reductions for investments and improvements that they would have undertaken anyway in the absence of the credits. For a full discussion of these issues, please refer to Items 2.05 and 2.06 below.

5. Inadvertent Effects
As mentioned above, since its inception, the Blue Collar Jobs Credits has been expanded several times and is sometimes identified as a program in which this incremental approach may have resulted in unanticipated shortcomings. Please refer to Items 2.05, 2.06, and 2.08 for a full discussion of possible inadvertent effects.

1.10 Military Action Exemption

1. Statutory Provision
Title 30, Delaware Code, Chapter 11, §1171.

2. Description
Income earned by U.S. Armed Forces personnel while on active duty who die from disease or injuries incurred while serving in a combat zone is exempt

from the personal income tax. Unpaid outstanding tax liabilities of such individuals are forgiven.

Additionally, income earned by U.S. Armed Forces personnel located outside the United States who die in "terroristic or military actions" is exempt from the personal income tax.

3. Estimated Revenue Loss
FY 19: Negligible
FY 20: Negligible

4. Assessment
This preference reaches its policy objectives in a fiscally effective manner. Even though the recent years have seen U.S. forces deployed in large numbers, the cost of this preference remains low. This is true because:

(1) Delaware is a small state, and its citizens constitute only a small fraction of the total military compliment;

(2) Members of the armed forces have discretion in determining their residence. A significant number choose states like Texas and Florida, which do not levy income taxes; and,

(3) Compared to other wars, such as World War II, Korea, and Vietnam, the number of casualties suffered in recent years has been relatively small.

Barring a major military engagement, war, or terrorist action overseas resulting in a much larger number of casualties, the cost of this preference will remain negligible.

5. Inadvertent Effects
None noted.

1.11 Extension of Filing Deadline for Military Personnel or Support Staff Serving in a Combat Zone

1. Statutory Provision
Title 30, Delaware Code, Chapter 3, §376.

2. Description
Military personnel who serve in a combat zone (pursuant to Section 112 of the IRC) are permitted to file their income tax returns up to 195 days after leaving the combat zone.

3. Estimated Revenue Loss
FY 19: Negligible
FY 20: Negligible

4. Assessment
Delaware's General Assembly implemented this provision in 1991 in response to Operation Desert Storm. Legislators recognized the practical difficulty of requiring military personnel to file a state personal income tax form while actively engaged in an overseas military operation.

This item is the most effective means of achieving its purpose fiscally and benefits those intended. The resulting impacts on final payments and refunds are minor. This provision is included as a tax preference because the filing deadline extension functions as a tax deferral in cases where a payment is due with the final return. While the deferral of final payment may amount to an interest-free loan from the state to the taxpayer, it is likely that many reservists' wage withholding levels were not adjusted to compensate for lower earnings during military service. In these cases, this filing deadline extension may actually result in the deferral of refund checks.

5. Inadvertent Effects
None noted.

1.12 Exemption for Retirement Distributions Used for Education

1. Statutory Provision
Title 30, Delaware Code, Chapter 11, §1106(b)(8).

2. Description
This preference allows an exemption from taxable income for early distributions from qualified retirement and deferred compensation plans, provided that the distribution is used in the same tax year to pay for books, tuition or fees at an institution of higher education. This exemption is available if the distribution is used to pay for costs incurred by the taxpayer receiving the distribution or any of the taxpayer's dependents under the age of 26.

3. Estimated Revenue Loss
FY 19: $2.4 million – $3.2 million
FY 20: $2.6 million – $3.4 million

4. Assessment
The purpose of this exemption is to provide parents of college age children with an additional alternative for funding their child's education. It assumes that the saving rate among families for their children's college education is insufficient. The provision's marginal impact is difficult to isolate, but it is likely minimal given all the financial considerations that affect college-funding decisions.

For example, consider a joint return filer in the 24.0% federal tax bracket. In the absence of this provision, this taxpayer would face a combined state and local marginal tax rate on early distributions from retirement plans of 30.6% in tax year 2018 (24.0% federal income tax rate + 6.6% state income tax rate). By allowing an exclusion for state tax purposes, the marginal rate facing this hypothetical taxpayer is reduced to 23.8% (a 21.6% reduction – 6.6%/30.6%). The degree to which such a reduction increases the use of retirement funds for higher education costs is uncertain.

5. Inadvertent Effects
Nationally, 72.5% of taxpayers who made deductible contributions to individual retirement accounts had adjusted gross incomes of $50,000 or more in 2016, according to IRS data. Low income families are most likely to need assistance with higher education costs, but they are also likely to have less money invested in retirement funds. This provision may benefit high income families disproportionately.

Additionally, to the extent that the provision does encourage the use of retirement funds for higher education costs, the amount available for distribution after retirement is reduced. Because the income from qualified distributions from tax deferred retirement vehicles is included in adjusted gross income, the use of retirement funds for higher education costs could reduce the amount available for retirement and the tax revenues these funds would generate.

1.13 Exemption for Trusts Established as "Designated" or "Qualified" Settlement Funds

1. Statutory Provision
   Title 30, Delaware Code, Chapter 16, §1633(4).

2. Description
   This provision exempts from Delaware income taxes the earnings of trusts that are recognized as "designated" or "qualified" settlement funds IRC §468B. Generally speaking, these types of settlement funds are established to satisfy claims arising out of tort, breach of contract, injury, death, property damage or violation of the law. *Designated* settlement funds may only be established by courts. *Qualified* settlement funds may be established by any government agency or instrumentality.

   IRC §468B(b)(3) exempts "qualified payments" to a designated settlement fund, defined as money or property transferred to a fund pursuant to a court order, from the fund's gross income. Treasury Regulations Section 1.468B-2 exempts "amounts transferred to the qualified settlement fund...to resolve or satisfy a liability for which the fund was established" from gross income. In the absence of this provision, trust income for state tax purposes would include any income other than transfers to pay claims, such as interest income from fund assets.

3. Estimated Revenue Loss
   FY 19: Unknown
   FY 20: Unknown

4. Assessment
   This preference is intended to further Delaware's reputation as a leader in the financial services sector. Since these funds are established by agreement between plaintiffs and defendants in civil cases, the prospect of taxation in Delaware would make it very likely that the parties to a suit would seek to establish such a fund outside the state. How successful this preference has been in achieving its intended purpose is unknown.

   It is likely that any funds which are located in Delaware due to this exemption would not be located here in the absence of this preference. Therefore, the state would not likely stand to gain additional revenue if it were to eliminate the credit.

5. Inadvertent Effects
None noted.

1.14 Land and Historic Resource Tax Credit

1. Statutory Provision
Title 30, Delaware Code, Chapter 18, §§1801 – 1807.

2. Description
This preference allows an income tax credit for permanent gifts of land or interest in land to public agencies and qualified private non-profit charitable organizations. Lands that qualify must either:

(1) meet the criteria for Open Space established by the Delaware Land Protection Act;

(2) Consist of natural habitat for the protection of Delaware's unique and rare biological and natural resources; or,

(3) Protect Delaware's important historic resources.

The tax credit is based on 40% of the appraised fair market value of the gift. The amount of credit that can be claimed is limited to $50,000. In any one tax year, the credit claimed cannot exceed the tax due, but unused portions of the $50,000 credit can be carried forward for up to five (5) consecutive years. The credit became available on January 1, 2000.

3. Estimated Revenue Loss [8]
FY 19: (D)
FY 20: (D)

4. Assessment
The goal of this tax preference is to encourage land conservation and historic preservation by providing an income tax preference for the donation of lands to the state or qualifying conservation organizations.

The state will have limited control over the types of land donated and the location of such land (subject to limitations discussed above) and no control

[8] The maximum amount that can be awarded in any one year cannot exceed $1 million, and these credits may not total more than $10 million over the life of the program.

(D) = Per 30 Del. C. §368, the Department of Finance is prohibited from disclosing tax return information identifying specific taxpayers. For additional information on the qualified donations in the Open Space program, please see https://dnrec.alpha.delaware.gov/parks/open-space/.

over the timing of such donations. As an alternative, the state could make outright purchases of properties deemed desirable for conservation. This approach would avoid an additional complication of the tax code and restore some degree of control and predictability to land conservation efforts.

5. Inadvertent Effects

In effect, through the adoption of this preference, the state is attempting to address a perceived market failure: the loss of open space. Like many business development incentives, a common criticism of awarding tax breaks for conservation efforts is that, in many instances, the desired behavior would have occurred in the absence of the tax break. That is, many of the land-owners who choose to participate in this program may have never contemplated developing their land. In such instances, this provision acts as a "bonus" and not as an incentive that actually changes behavior.

Whether the value of preserving open space exceeds the benefits of allowing market forces to determine the lands' "highest and best" use is debatable. If open space preservation efforts are extensive enough they could influence real estate markets by increasing housing prices in certain areas.

1.15 Historic Preservation Credit

1. Statutory Provision

Title 30, Delaware Code, Chapter 18, §§1811 – 1817.

2. Description

Under this provision, a person who wishes to repair or otherwise preserve a historic property may apply to the State Historic Preservation Office, for a partial credit for qualified expenditures.

To qualify for the credit, an individual must first submit a rehabilitation proposal to the Historic Preservation Office to ensure that the restoration, when completed, would meet federal and state guidelines. Credits would be granted on a first come-first serve basis, not to exceed $8 million[9] in any one fiscal year. Moreover, of the credits awarded in a given fiscal year, $100,000 must be reserved for distribution to qualified resident curators; $1.5 million shall be reserved for projects receiving a credit of not more than $300,000, and $1.5 million shall be reserved for projects located in Downtown Development Districts.

[9] The maximum amount of credits awarded shall not exceed $8 million for Fiscal Years 2020-2025 (82 Del. Laws c. 86 § 46).

Upon project completion, a State Preservation Office must certify that the end product conforms to federal and state requirements. Once certified, the Division of Revenue or the Office of the State Bank Commissioner will determine the appropriate value of the tax credit to be issued. Personal/corporate income or bank franchise tax credits may be valued at:

- 20% (30% in the case of low income housing) of qualified expenditures made in the rehabilitation of any certified historic property eligible for a federal tax credit under §47 of the Internal Revenue Code (income producing properties);

- 30% (40% in the case of low income housing) of qualified expenditures made in the rehabilitation of any certified historic property not eligible for a federal tax credit under IRC §47 (non-income producing properties); or

- 100% of the qualified expenditures made in the rehabilitation of a certified historic property qualifying for credit award as a resident curatorship property regardless of eligibility for a federal tax credit under IRC §47 [26 U.S.C. §47].

Rehabilitative efforts taking the following forms do not qualify for the Historic Preservation Credit:

1) The acquisition of real property or interest in real property,

2) Additions to existing structures when the square footage of all additions is greater than or equal to 20% of the total square footage of the historic portion of the property,

3) Paving or landscaping costs that exceed 10% of the total qualified expenditure,

4) Sales and marketing costs, or,

5) Expenditures not properly charged to a capital account, or, in the case of owner occupied property, would not be charged to a capital account if the owner were using such property in a trade or business.

3. Estimated Revenue Loss[10]
   FY 19: $925,000
   FY 20: $1,500,000 - $1,700,000

4. Assessment
   The intention of this provision is to encourage private sector participation in maintaining and preserving the state's historic structures. However, since no public purpose is required for participation in this program, it is possible that the benefits enjoyed from this credit could accrue to relatively few and most likely wealthy individuals. Credits could be issued for renovations conducted on privately owned homes located in isolated areas. In these instances, taxpayers subsidizing the historic renovation would be unable to even view that for which their tax dollars have paid. Recent experience, however, has proven that businesses account for the majority of those qualifying to take this credit.

   Additionally, it is unlikely that individuals with insufficient means to undertake renovations would be motivated by this tax incentive. As such, it is possible that this credit may act more as preservation subsidy than as a preservation incentive.

   Because this preference is administered on a first-come, first-served basis, it would also be possible for funds which should have been allocated to the state's most important historic resources to instead be diverted to other, potentially less worthy, properties. Moreover, this method of allocation may cause equity concerns given that there is no restriction on the amount of tax credit than can be granted to any one taxpayer. Consequently, one taxpayer could receive the entire $8 million credit allotment in any given year.

5. Inadvertent Effects
   As previously mentioned, aside from the resident curator provision there is nothing preventing one large taxpayer from receiving the remainder of the credits available in any given fiscal year. Such allocation of the credit may actually hinder preservation efforts by causing individuals who would have otherwise begun historic rehabilitation to postpone projects until the credit is once again available. Additionally, equity concerns are a likely consequence of credit monopolization.

[10] Claims against tax credits may not be taken until approved projects are completed.

1.16 Earned Income Tax Credit

1. Statutory Provision
   Title 30, Delaware Code, Chapter 11 §1117.

2. Description
   Federal law permits certain low-income individuals with earned income, meeting adjusted gross income thresholds, to take a refundable Earned Income Tax Credit (EITC). Starting with Tax Year 2006, Delaware taxpayers who qualify to take the federal EITC are permitted to take a non-refundable state tax credit equal to 20% of the federal amount.

3. Estimated Revenue Loss
   FY 19: $12.5 million
   FY 20: $13.6 million

4. Assessment
   EITC advocates consider this credit to be an important tool in fighting poverty. Since 1975, the federal Earned Income Tax Credit has worked as an income subsidy which is delivered through the tax code and targets the working poor. As opposed to traditional welfare programs, proponents argue that the EITC encourages socially beneficial behavior by rewarding work.

5. Inadvertent Effects
   Among federal tax preference items, the EITC has one of the higher rates of errors and noncompliance. Because the federal EITC is a refundable credit, the impact of these errors and noncompliance frequently exceed the amount of federal tax otherwise due. Delaware has attempted to limit the state's financial exposure in this respect by issuing only non-refundable credits. Delaware's experience administering its EITC is largely consistent with the federal track record. As a consequence, the administration of the EITC, an effective low-income subsidy, appears to come at a somewhat higher administrative cost relative to the cost of other tax preference items.

1.17 Exemption of Out-of-State Resources During Declared Emergencies

1. Statutory Provision
   Title 30, Delaware Code, Chapter 31, §§3101 – 3105.

2. Description
Delaware does not consider equipment and personnel employed during a declared state of emergency by infrastructure companies based in other states to constitute legal presence in the state for tax purposes if those assets are employed in emergency related work.

3. Estimated Revenue Loss
FY 19: Negligible
FY 20: Negligible

4. Assessment
This preference may facilitate the response to future disasters by eliminating tax concerns of companies employing out-of-state resources. Firms will not be required to calculate and submit income tax withholdings for out-of-state individuals conducting infrastructure work during a declared emergency period. This may remove a potential barrier to bringing those individuals into the state.

The revenue lost from this preference is likely to be negligible for two reasons. First, the probability of a declared disaster occurring during any given fiscal year is small and unpredictable. Second, enforcement would likely be low if Delaware chose to tax this activity.

5. Inadvertent Effects
None noted.

1.18 Vocational Rehabilitation Hiring Credit

1. Statutory Provision
Title 30, Delaware Code, Chapter 20B, §§20B-100 – 20B-104.

2. Description
This preference provides an incentive for employers to hire individuals with a state certified physical or mental disability who are in the process of, or have completed, vocational rehabilitative services. Employers may claim a refundable credit against the bank franchise tax, corporate income tax, personal income tax, or insurance income tax equal to 10% of gross wages or $1,500, whichever is lower, for each qualified disabled worker they hire. Credits may be claimed in the year the qualified disabled worker is hired and for two subsequent years.

3. Estimated Revenue Loss
FY 19: $0
FY 20: Negligible

4. Assessment
The credit is available for hiring occurring on or after January 1st, 2017 and may be taken in the year of the hiring and up to two years thereafter. The tax credit can provide a labor market advantage for individuals with a qualified disability to offset other employment disadvantages they might face.

5. Inadvertent Effects
Employers taking this credit may already employ individuals with a qualified disability and receive the federal WOTC. In these cases, the Vocational Rehabilitation Hiring Credit acts as a bonus rather than an incentive. Additionally, the record retention requirements of this credit increase the complexity of the tax return. As returns become more complicated, more errors are made when filing and more administrative costs are incurred during the tax verification process.

As a credit that overlaps with other federal incentives, it is important to note that any attempt to mirror the federal provisions on a piecemeal or incremental basis may mask fiscal impacts when evaluated independently. However, when combined, the impact of all preferences may be significant. While the goal of incentivizing work opportunities for the disadvantaged is a laudable one, achieving such a goal through direct appropriation or via a single tax preference linked to the federal WOTC would be simpler and more transparent.

1.19 Angel Investor Tax Credit

1. Statutory Provision
Title 30, Delaware Code, Chapter 20D, §§20D-101 – 20D-110.

2. Description
This preference provides an incentive for investors to invest capital in qualified Delaware-based, high-tech small businesses. Qualified investors can claim a refundable tax credit of 25% of their qualified investment. The total credits awarded per year is capped at $5 million. The cumulative tax credit limit for qualified investors in one year is $250,000 for married couples filing jointly, $125,000 for individuals. No more than $500,000 in credits may be awarded for qualified investments in any one qualified business over all

calendar years. This provision expires for tax years convening on of after January 1, 2022.

3. Estimated Revenue Loss
FY 19: N/A
FY 20: (D)

4. Assessment
The purpose of the tax credit is to create an environment that supports small, high tech businesses, increases their access to capital, encourages companies to plant their "roots" in Delaware, grows the Delaware economy, and creates an environment that is attractive to new investment in the long term. Investors must maintain their investments in the business for three calendar years. If an investor fails to maintain investments in the business for the full three-year period, the tax credit may be revoked; if it is revoked, the credit must be repaid to the state in full. If a business fails to maintain certain expenditure and employment requirements over the three-year period, the tax credit is revoked and must be repaid to the state according to a repayment schedule (prorated 100%, 66.7% and 33.3%, depending on the number of years for which these requirements were met).

5. Inadvertent Effects
None noted.

(D) = Per 30 Del. C. §368, the Department of Finance is prohibited from disclosing tax return information identifying specific taxpayers. For additional information on the Angel Investor Tax Credit, please see the annual report from the Division of Small Business, as required by 30 Del. C. § 20D-107(f).

CORPORATE INCOME TAX

- Statutory Provision

  Title 30, Delaware Code, Chapters 19 and 64.

- Collection/Administrative Agency

  The Department of Finance, Division of Revenue, administers this tax.

- General Liability

  Every domestic and foreign corporation doing business in Delaware is required, unless specifically exempt by law, to file a corporate income tax return regardless of the amount of its gross income or its taxable income. Corporations that maintain a statutory office in Delaware but do not conduct business within the state are not required to file a corporate income tax return.

  Tax liabilities for Delaware purposes are based on the share of the corporation's federal taxable income that is allocated and apportioned to Delaware. Delaware taxable income does not include interest on obligations of the United States, the state of Delaware, or its subdivisions. Dividends, interest, and royalties of foreign corporations that qualify for a foreign tax credit for federal purposes are excluded from Delaware taxable income. Additional deductions are allowed for wages eliminated as a deduction in the calculation of the federal Jobs Credit and certain expenditures on renovations that improve accessibility for handicapped persons.

  Income from rents and royalties, patents and copyright royalties, gains and losses from the sale or other disposition of real and tangible personal property, and interest is allocated directly to the states where the property is physically located or the transactions took place, reduced by the applicable related expenses.

  Apportionment of unallocated income has historically been based on a three-factor formula (see below) that averages the ratios of: 1) Delaware property to total United States property; 2) Delaware wages to total United States wages; and 3) Delaware gross receipts to total United States gross receipts for interstate businesses. Non-U.S. corporations may not use property or payroll without the United States of America to dilute their payroll and property apportionment factors. The apportionment formula is applied to a company's entire taxable income, excluding its allocated and exempt income.

As a result of the Delaware Competes Act, signed into law on January 27, 2016, the apportionment calculation is transitioning to a single factor based solely on gross receipts as reflected in the table below.

2016 and years prior	Apportionment Ratio = .333 * Property Ratio + .333 * Salary Ratio + .333 * Sales Ratio
2017	Apportionment Ratio = .25 * Property Ratio + .25 * Salary Ratio + .50 * Sales Ratio
2018	Apportionment Ratio = .20 * Property Ratio + .20 * Salary Ratio + .60 * Sales Ratio
2019	Apportionment Ratio = .125 * Property Ratio + .125 * Salary Ratio + .75 * Sales Ratio
2020 and beyond	Apportionment Ratio = Sales Ratio

- Tax Rate
  8.7% of taxable income

- Tax Receipts, net of refunds (millions of dollars)

Fiscal Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total ($)	87.9	168.3	119.1	187.9	102.0	269.5	143.3	120.8	89.7	147.8

- Tax Preferences
  The following table identifies corporate income tax preferences within the Delaware Code along with annual estimated costs. Links within the table navigate to more detailed analysis of each tax preference.

TAX PREFERENCE	FY 19 (EST)	FY 20 (EST)
2.01 Exemption of Investment Holding Companies, Firms Managing Intangible Investments of Mutual Funds	Unknown	Unknown
2.02 Deduction of Interest from Affiliated Companies	Negligible	Negligible
2.03 Handicapped Accessibility Deduction	Negligible	Negligible
2.04 Neighborhood Assistance Credit	$250,000 - $350,000	$500,000 - $700,000
2.05 Tax Credit for Creation of Employment and Qualified Investments in Business Facilities (New Jobs Creation formerly Blue Collar Jobs Act)	(D)	(D)
2.06 Tax Credit for Creation of Employment and Qualified Investments in Targeted Areas (New Jobs Creation formerly Blue Collar Jobs Act)	Negligible	$50,000 - $100,000
2.07 Clean Energy Technology Device Manufacturing Tax Credits	$0	$0
2.08 Credits for Development at "Brownfield" Sites and Facilities	$0	$0
2.09 Research and Development Tax Credit	$19.0m	$15.0m
2.10 Land and Historic Resource Tax Credit	(D)	(D)
2.11 Historic Preservation Credit	$1.7 - $1.9m	$1.2 - $1.6m
2.12 Headquarters Management Company	$0	$0
2.13 Asset Management Corporation	Negligible	Negligible
2.14 Business Finder's Fee Tax Credit	$0	$0

2.15 Veterans' Opportunity Credit	$0	N/A
2.16 Exemption of Out-of-State Resources During Declared Emergencies	Negligible	Negligible
2.17 New Economy Jobs Tax Credit	$0	$0
2.18 Vocational Rehabilitation Credit	Negligible	Negligible
2.19 Apportionment Election Preference for Worldwide Headquarters and Telecommunications Companies	(D)	(D)
2.20 Automatic External Defibrillator Tax Credit	Negligible	Negligible

(D) = Per 30 Del. C. §368, the Department of Finance is prohibited from disclosing tax return information identifying specific taxpayers.

2.01 Exemption of Investment Holding Companies, Firms Managing Intangible Investments of Mutual Funds

1. Statutory Provision
   Title 30, Delaware Code, Chapter 19, §1902(b)(8).

2. Description
   Investment holding companies and corporations whose activities within this state are confined to the maintenance and management of the intangible investments of corporations or business trusts registered as investment companies under the Investment Company Act of 1940 are exempt from the corporate income tax.

3. Estimated Revenue Loss
   FY 19: Unknown
   FY 20: Unknown

4. Assessment
   This provision is designed to spur economic development in the state. The tax preference is intended to strengthen the state's reputation as a major financial center and to signal to the financial community that Delaware is a progressive state in terms of liberalizing its financial regulatory environment. Originally, this exemption applied only to investment holding companies. On July 1, 1990, this provision was extended to include corporations that invest the funds of a mutual fund.

   Eligible firms file informational returns establishing their eligibility for the exemption and do not have to file a corporate income tax return. This makes an accurate assessment of the revenue impact of this provision little more than guesswork. Investment holding companies are established in Delaware primarily because of this tax exemption, and it is likely that many of them would leave the state if the exemption were repealed or modified given the mobility of intangible assets. No data exist by which the Division of Revenue could make its own estimate of the revenue loss generated by this exemption.

   In recent years, many states have passed legislation to effectively prevent companies from deducting expenses paid to Delaware Investment Holding Companies from corporate income. As the number of states which allow these payments to be deducted from corporate income decreases, the use of these companies may potentially decrease as well.

5. Inadvertent Effects
None noted.

2.02 Deduction of Interest from Affiliated Companies

1. Statutory Provision
Title 30, Delaware Code, Chapter 19, §1903(a)(2).

2. Description
Delaware allows firms (creditors) to deduct the amount of interest income (including discount) that they earn on inter-corporate obligations, usually in the form of advances, loans, or similar contractual transactions. In order to qualify for this deduction, the following requirements must be met:

(i) the debtor and creditor corporations are subject to taxation under Delaware law; and,
(ii) the debtor corporation does not claim a deduction for such interest payments in determining its entire net income for Delaware corporation income tax purposes.

3. Estimated Revenue Loss
FY 19: Likely to be Negligible*
FY 20: Likely to be Negligible*

* Accounts for a very high probability of a sweeping behavioral effect. See discussion in Assessment, below.

4. Assessment
The corporate income tax deduction for interest from affiliated corporations allows related companies to shift interest income and related expenses among members of a group that is eligible to file a federal consolidated return. The rationale behind this provision is consistent with the idea behind the exemptions for investment holding companies (Item 2.01) and designated or qualified settlement funds (Item 1.13). A tax advantage for the management of inherently mobile intangible assets, such as inter-company obligations, enhances Delaware's reputation as a financial center and may also produce relatively small employment gains for Delaware's financial and legal communities. Because the ease with which intangible assets could be moved from Delaware is so great, it is clear that a tax incentive's impact on the decision to locate such assets in Delaware is critical.

In fact, many argue that a business's decision to "locate" intangible assets in Delaware occurs solely due to the tax incentive. Unlike tangible business assets, such as a production or research facility, the location of intangible assets is not dependent upon the quality of public infrastructure, access to markets, a well-trained pool of labor, or quality of life considerations. In the event of its repeal, the vast majority of the intangible assets covered under this provision would leave the state, drastically reducing any revenue loss estimate produced on a static basis.

When the deduction was enacted in 1957, Delaware permitted corporations to elect to file consolidated returns. Since most corporations at that time filed consolidated returns, there was little or no revenue impact resulting from the shift of income among related companies. Starting on August 1, 1971, however, corporations were not permitted to file consolidated returns and now must file a separate return for each corporation conducting business within Delaware. Interest may be excluded from state taxation to the extent that the creditor corporation (the corporation that receives the interest income) conducts a greater percentage of its business in Delaware than the debtor corporation (the corporation that pays the interest on its debt).

Affiliated finance companies (AFCs) present a special case under this tax preference. The AFC acts as a creditor by purchasing receivables from their affiliate or "core business" (a large retailer, for example). The affiliate usually has a very small apportionment percentage because sales in Delaware make up only a small part of its market. The AFC, however, usually has a very high apportionment percentage (frequently 100%). The interest on a large loan from an AFC to the core business is often sufficient to totally eliminate its tax liability when deducted from the AFC's net income. The AFC's primary function is to enhance the financial position of the core business; large loans are not uncommon. It is evident that this preference is the reason behind the establishment of AFC's in Delaware. The fact that so many AFC's were established in Delaware in response to this provision suggests that its elimination would cause many or all AFC's to move to other states.

As mentioned above, estimates of the revenue loss for this tax preference are confounded by unknown market responses to a change in this tax law. Although the elimination of this provision could cause a temporary, short-term increase in revenues, firms likely would move these operations out of the state as quickly as possible, erasing any long-term revenue gain.

5. Inadvertent Effects
None noted.

2.03 Handicapped Accessibility Deduction

1. Statutory Provision
Title 30, Delaware Code, Chapter 19, §1903(a)(2).

2. Description
Delaware offers a deduction, not to exceed $5,000, equal to the renovation expenses incurred removing design features in a building which restrict a physically handicapped person's full use of said building. For the purposes of this provision, Delaware Code defines "building" as building or structure, located in Delaware and open to the general public. This definition includes sidewalks, curbing, driveways, and entrances connected with, or related to, the use of the building structure. Expenditures incurred in the removal of architectural barriers or physical design features in order to make the building more accessible to handicapped individuals also qualify.

3. Estimated Revenue Loss
FY 19: Negligible
FY 20: Negligible

4. Assessment
This deduction is rarely utilized; in most years, no firms use the preference. This suggests that it is insufficient to encourage businesses to undertake costly renovations. This is true despite the fact that the deduction may be claimed in addition to a deduction on depreciation for renovation projects. Moreover, corporations are also allowed to expense up to $15,000 of capital costs in lieu of depreciation to remove architectural and transportation barriers to handicapped individuals under §190 of the federal IRC, which is adopted by Delaware law. As such, corporations may receive a Delaware tax benefit of up to $435 (8.7% of the capital project up to $5,000) in addition to expensing or depreciating the capital investment.

Small businesses may also claim the federal "disabled access tax credit" equal to 50 percent of "eligible access expenditures" (defined under Section 44 of the IRC) that exceed $250 but not exceeding $10,000. To be eligible, a small business must have gross receipts of less than $1 million or no more than 30 full-time employees.

Despite these federal and state inducements, very few companies have responded to them. The primary policy tool in promoting handicapped accessibility is the Americans with Disabilities Act (ADA). Enforcement of the ADA depends primarily upon private lawsuits brought by persons who claim that a business is non-compliant.

Given its history of limited use, it appears that utilization of this tax benefit will remain inconsequential and that this provision will do little to achieve its intended purpose. It is also unclear whether the state should subsidize actions that are already mandated by other laws.

5. Inadvertent Effects
None noted.

2.04 Neighborhood Assistance Credit

1. Statutory Provision
Title 30, Delaware Code, Chapter 20, Subchapter I, §§2001 – 2007.

2. Description
Persons that invest in community development programs approved by the Director of the Delaware State Housing Authority and the Neighborhood Assistance Act Advisory Council are entitled to a tax credit equal to fifty percent (50%) of the amount invested by a business firm in a program or in a Community-Based Development Organization. The tax credit is limited to the lesser of 50% of a firm's qualifying investment or $50,000. The aggregate amount of tax credits awarded in any one year may not exceed $1 million.

The term "Neighborhood Assistance" encompasses contributions to neighborhood organizations, Community Development Corporations, or Community-Based Development Organizations, which fund the following activities: job training or education for individuals not employed by the business firm, community services, crime prevention, housing, or economic development in an impoverished area.

Legislation enacted during the 147th General Assembly reduced the maximum annual award of Neighborhood Assistance Credits and capped the amount a firm may receive over a three year period in order to extend the availability of the credit to a greater number of firms.

3. Estimated Revenue Loss
FY 19: $250,000 - $350,000[1]
FY 20: $500,000 - $700,000[2]

4. Assessment
The goal of this credit is to encourage Delaware businesses to invest in job training, education, crime prevention, and other community services in designated impoverished areas.

5. Inadvertent Effects
None noted.

2.05 Tax Credit for Creation of Employment and Qualified Investments in Business Facilities (New Jobs Creation formerly Blue Collar Jobs Act)

1. Statutory Provision
Title 30, Delaware Code, Chapter 20, Subchapter II, §§2010 – 2015.

2. Description
Any corporate taxpayer that makes a qualified investment ($200,000 or more) and that hires five or more qualified employees ($40,000 per employee) is entitled to receive a tax credit. Eligible corporations receive credits of $500 for each qualified employee and $500 for each $100,000 invested, not to exceed fifty percent of their tax liability in a given year. Credits may be taken in the taxable year in which all eligibility conditions are met and for any of the 9 following taxable years. Unused credits may be carried forward.

Qualified activities are defined as:

1. Manufacturing;
2. Wholesaling;
3. Scientific, agricultural or industrial research development or testing;
4. Computer processing, or data preparation and processing services;
5. Engineering services;
6. Consumer credit reporting services, including adjustment and collection services and credit reporting services;
7. Telecommunications services;
8. Aviation services;

[1] Includes revenue loss due to credits claimed under the personal income tax by pass-through entity partners/owners.
[2] Increase is a result of legislation enacted in 2018 increasing the aggregate credits authorized from $500,000 to $1,000,000.

9. Non-custom computer software;
10. Any combination of the activities described above; or,
11. The administration, management or support operations (including marketing) of any activity described above.

Telecommunication service businesses are required to hire at least 50 qualified employees and make a minimum investment of $15,000 per qualified employee (with a minimum aggregate investment of $750,000, rather than $200,000).

An alternative investment tax credit of $375 per $100,000 of investment is available in cases where the qualified investment is at least the greater of $1 million, or 15% of the unadjusted basis of the qualified facility. The alternative credit is to be used by manufacturers, wholesalers or aviation service firms who do not meet the ordinary requirements for investment credits, such as the required number of new employees).

Eligibility for corporate income tax credits also means firms become eligible for gross receipts and public utility tax breaks.[3] Unused credits may be carried forward for use in future tax years.

Both corporate income tax receipts and the cost of this preference fluctuate considerably from year to year.

3. Estimated Revenue Loss[4]
FY 19: (D)
FY 20: (D)

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[3] A related type of investment credit can be used against the bank franchise tax (5 Del. C., Chapter 11, Section 1105(h)-(i)).

[4] This estimate only includes the fiscal impact of this provision with respect to the corporate income tax. No assessment is made of the extent to which these credits will be claimed against other eligible taxes. Given this limitation, the fiscal impact estimate does not reflect the full impact of this provision on state revenues. It also excludes any "dynamic" revenue effect the credit may have (i.e., economic improvements resulting from the credit which offset some of its cost). For example, to the extent that the qualified investment in new facilities and employees increases a firm's productivity (and profits) corporate income tax receipts – and other state tax receipts – could increase. Establishing and quantifying a causal effect, however, would be tenuous at best.

(D) = Per 30 Del. C. §368, the Department of Finance is prohibited from disclosing tax return information identifying specific taxpayers.

4. Assessment

The first goal of these credits is to promote job creation and investment in Delaware by giving employers incentives to hire additional full-time employees or to expand business facilities. The second goal is to offer an incentive to firms that are considering whether to locate a facility in Delaware. Whether a $500 credit per $100,000 of investment (0.5%) offers enough incentive for firms to expand is an open question, but appears improbable. In the absence of increased demand for a firm's products or services, the promise of a relatively small tax subsidy will make little difference in the expansion decision.

These credits also attempt to create a competitive environment to attract new business to Delaware. State development officials have indicated that these credits serve a useful role as a marketing tool in recruiting new businesses to Delaware. On the margin, the existence of tax credits may tip a firm's location decision in Delaware's favor. The credits may have value if they portray Delaware as being committed to economic development.

In general, though, the impact of taxes on business location decisions is often of secondary importance to other elements of a state's business climate. Access to markets, labor skill and supply, and infrastructure quality are typically more important considerations in a business's location decision. It is often unclear whether tax credits are critical to a firm's decision to establish or expand its operations in Delaware or if they merely serve as a bonus to firms that would have chosen to locate here regardless of the credit. The size of the incentives suggests that they are unlikely to have a significant impact on businesses' location decisions. Despite this, proponents argue that such credits must be offered for businesses to even consider Delaware as a potential location. Although the credits often may not be *the* deciding factor in a location decision, they still may be an important consideration. The marginal impact of the credits may be important enough to retain them; they may even be considered a cost of doing business for state development efforts.

An assessment of the fiscal impact of the credits depends on the ability to identify those business decisions that were influenced by the credits and those that were not. Fiscal impacts could then be calculated for both sets of decisions and weighed against each other. However, no data exist that would allow such a comparison to be conducted.

5. Inadvertent Effects
These credits may indeed serve as a useful promotional tool for state development officials. However, there is an equally strong probability that most firms are simply "rewarded" with a bonus for actions that they would have taken without the existence of a credit, rather than "earning" a credit for actions that would not have occurred without them.

2.06 Tax Credit for Creation of Employment and Qualified Investments in Targeted Areas (New Jobs Creation formerly Blue Collar Jobs Act)

1. Statutory Provision
Title 30, Delaware Code, Chapter 20, Subchapter III, §§2020 – 2022.

2. Description
This provision provides employers engaged in qualified activities (as defined in §2010 – see above) an extra credit of $250 (for a total credit of $750) for each additional full-time employee, and an extra credit of $250 (for a total of $750) for each $100,000 investment in qualified facilities located in "targeted areas" (as defined in §2020), in addition to the credits allowable under §2011 above.

A related credit of $500 (the amount for investment in qualified facilities) is allowed for facilities engaged in "commercial or retail activity" within targeted areas. *Commercial activities* (as defined in §2020(1)) include all services except: amusement conductor, amusement park operator, auctioneer, automobile race operator, bowling alley operator, circus exhibitor, entertainment agent, finance or small loan agency, floor show operator, health spa or health club, junk dealer, motion picture theater, outdoor music festival promoter, pawnbroker, pool table operator, public bath keeper, salvage yard operator and self-service laundry or dry cleaner. *Retail activities* (as defined in §2020(2)) include all retail trade except: providing retail food and beverage services (including eating and drinking places, but excluding grocery and convenience stores), engaging in automobile sales, or providing recreation or entertainment. Facilities meeting this expanded definition in targeted areas are treated as if they qualified for the credit described above in 2.05.

3. Estimated Revenue Loss [5]
FY 19: See Item 2.05 above
FY 20: See Item 2.05 above

[5] This figure is included in the fiscal impact estimate for tax credits for the creation of employment and qualified investment in business facilities (Item 2.05).

4. Assessment
These credits were established to further encourage economic development and employment in underdeveloped areas of the state and to create a business environment that is competitive with other states in the region. It is likely that some of the financial benefit of these credits accrues to firms that would have invested in these areas anyway. In these cases, the use of this preference does not reflect behavioral change induced by the tax benefit; the credits are of secondary importance to other elements of a state's business climate, such as access to markets, the skill and cost of labor, and infrastructure. Given the size of the incentives and the characteristics of the targeted areas, they seem unlikely to have a significant impact on business location decisions.

5. Inadvertent Effects
Certain qualifying firms may be benefiting from a tax incentive for actions that were largely unrelated to the existence of the preference.

2.07 Clean Energy Technology Device Manufacturing Tax Credits

1. Statutory Provision
Title 30, Delaware Code, Chapter 20, §2040.

2. Description
Clean energy technology device manufacturers qualifying for the New Job Creation Credit (see Item 2.05) are entitled to increase the income tax credits established under that provision by $250, from $500 to $750. Clean energy technology device manufacturers include makers of the following items:

- Solar power devices;
- Fuel cells;
- Wind power devices; and,
- Geothermal power devices.

3. Estimated Revenue Loss[6]
FY 19: $0
FY 20: $0

4. Assessment
At present this credit has not been claimed.

[6] While these credits have not been used in previous years, their use may grow in the future as Delaware's manufacturing landscape changes.

This credit was established to further encourage economic development and employment with respect to specific forms of manufacturing within the state. While this credit has not been used so far, it may potentially be utilized in the future should clean energy manufacturing become increasingly popular. Like all economic development credits, it is likely that some of the financial benefit of these credits will ultimately accrue to firms that would have made the investments regardless of the credit.

5. Inadvertent Effects
See Items 2.05 and 2.06.

2.08 Credits for Development at "Brownfield" Sites and Facilities

1. Statutory Provision
Title 30, Delaware Code, Chapter 20, §2011(l).
Title 30, Delaware Code, Chapter 20, §2021(d).

2. Description
Brownfield properties are typically abandoned properties where some residual environmental contamination may still exist or where fears of cleanup liability may be preventing re-use of the land. Piggybacked on the New Job Creation Credits, the "brownfield" credits attempt to encourage redevelopment of these lands by offering reduced license fees and tax credits for firms that invest in these properties. Tax credits worth $650 for each qualified employee and $650 for each $100,000 in qualified investment in "brownfield" sites are available. The value of these credits grows to $900 per qualified employee or $900 for each $100,000 in qualified investments if the "brownfield" is also located in a "targeted" area as defined under §2020.

3. Estimated Revenue Loss
FY 19: $0[7]
FY 20: $0

4. Assessment
Since the inception of this program in 1995, this program has gone largely unused.

As with many tax preferences, the brownfield credits may not offer enough incentive to outweigh the large potential cleanup liabilities that investment in

[7] When relevant estimates include revenue losses due to credits claimed under the personal income tax by pass-through entity partners/owners.

or ownership of these properties may entail. Moreover, firms that would actually fund and oversee a brownfield clean up, such as those that specialize in environmental remediation or real estate development, would not typically meet the New Job Creation Credit employment, investment and qualified activity requirements. As mentioned above, Brownfield Credits can only be awarded if the firm first qualifies for the New Job Creation Credit.

Further diminishing the Brownfield credit's efficacy is the fact that otherwise eligible firms may not be initially profitable. Because of this, they have no corporate income tax liability and are often small enough to be exempt from payment of the gross receipts tax. The offer of a non-refundable tax credit is irrelevant to a firm without any tax liability within the foreseeable future.

5. Inadvertent Effects
Like other tax preferences that try to induce behavioral change, it seems likely that the brownfields credits will reward behavior that would have occurred regardless of the preference.

2.09 Research and Development Tax Credit

1. Statutory Provision
Title 30, Delaware Code, Chapter 20, Subchapter VIII, §§2070 – 2075.

2. Description
This preference, adapted from similar federal tax provisions, allows a credit against tax for qualified research conducted within Delaware. As a result of the Commitment to Innovation Act, signed into law March 17, 2016, this credit was amended to ensure that all companies receive the full research and development tax credit for which they qualify. Prior to tax year 2017, the statewide cap on such credits was $5 million per year. If statewide credit applications exceeded $5 million, receipts were allowed *pro rata* according to the approved amount so that the total approved credits would not exceed $5 million. For tax years 2017 and beyond, the Commitment to Innovation Act removes the $5 million cap and the full, approved amount of the credit will be granted.

This legislation also provides that credits issued for tax years 2017 and later will be refundable. Unused credits issued prior to tax year 2017 cannot be carried back but can be carried forward fifteen years; these credits remain nonrefundable.

3. Estimated Revenue Loss
FY 19: $19.0 million
FY 20: $15.0 million

4. Assessment
The purpose of this preference is to enhance Delaware's reputation as a home for research-intensive firms, such as pharmaceutical and biotechnology firms. Like all business tax incentives, it is difficult to isolate that portion which actually results in "new" economic activity from that part which merely serves as a bonus to firms that would have engaged in the desired activity in the absence of the incentive. Because the Research and Development Credit is used by many firms that already had significant research and development activity in Delaware prior to its enactment, it is likely that a large portion of the provision's cost does not add to the level of research and development conducted in Delaware. On the other hand, as may be the case with the New Job Creation Credits, the Research and Development Credits may be considered an unavoidable cost of doing business for states that hope to compete successfully in the area of high-tech economic development.

5. Inadvertent Effects
None noted.

2.10 Land and Historic Resource Tax Credit

1. Statutory Provision
Title 30, Delaware Code, Chapter 18, §§1801 – 1807.

2. Description
This preference allows an income tax credit for permanent gifts of land or interest in land to public agencies and qualified private non-profit charitable organizations. Lands that qualify must either:

(1) meet the criteria for Open Space established by the Delaware Land Protection Act;

(2) Consists of natural habitat for the protection of Delaware's unique and rare biological and natural resources; or

(3) Protect Delaware's important historic resources.

The tax credit is 40% of the appraised fair market value of the gift up to $50,000. The credit is not refundable, but unused portions can be carried forward for up to five (5) consecutive years.

3. Estimated Revenue Loss
FY 19: (D)
FY 20: (D)

4. Assessment
This credit may not be effective in motivating some corporate donors—this credit only benefits those firms that have a tax liability. Due to fluctuations in net corporate income, in any given year three-quarters of firms have little or no tax liability and would therefore have little incentive to take advantage of the credit.

For further discussion, refer to Section 1.14.

5. Inadvertent Effects
Refer to Section 1.14.

(D) = Per 30 Del. C. §368, the Department of Finance is prohibited from disclosing tax return information identifying specific taxpayers. For additional information on the qualified donations in the Open Space program, please see https://dnrec.alpha.delaware.gov/parks/open-space/.

2.11 Historic Preservation Credit

1. Statutory Provision
Title 30, Delaware Code, Chapter 18, §1813.

2. Description
Under this provision, a person who wishes to repair or otherwise preserve a historic property may apply to the State Historic Preservation Office for a partial credit for qualified expenditures.

To qualify for the credit, an individual must first submit a rehabilitation proposal to the Historic Preservation Office to ensure that the restoration will meet federal and state guidelines. Credits are to be granted on a first-come, first-served basis, not to exceed $5 million in any one fiscal year. Projects receiving a credit of not more than $300,000 are allocated at least $1.5 million of the total, and $1.5 million of credits are reserved for projects located in Downtown Development Districts, $500,000 of which is reserved for projects receiving a credit of not more than $300,000. Moreover, $100,000 of the credits awarded in a given fiscal year must be reserved for distribution to

qualified resident curators. After April 1 of each year, any unused balance from the reserved amounts is available for any eligible project.

Upon project completion, the State Preservation Office must certify that the end product conforms to federal and state requirements. Then the Division of Revenue or the Office of the State Bank Commissioner will determine the appropriate value of the tax credit to be issued. Personal Income Tax, Corporate Income Tax, or Bank Franchise Tax credits may be valued at:

- 20% (30% in the case of low income housing) of qualified expenditures made in the rehabilitation of any certified historic property eligible for a federal tax credit under §47 of the Internal Revenue Code (income producing properties);

- 30% (40% in the case of low income housing) of qualified expenditures made in the rehabilitation of any certified historic property not eligible for a federal tax credit under §47 of the Internal Revenue Code (non-income producing properties); or,

- 100% of the qualified expenditures made in the rehabilitation of a certified historic property qualifying for credit award as a resident curatorship property regardless of eligibility for a federal tax credit under § 47 of the Internal Revenue Code [26 U.S.C. § 47].

Rehabilitative efforts taking the following forms do not qualify for the Historic Preservation Credit:

1) The acquisition of real property or interest in real property;

2) Additions to existing structures when the square footage of all additions is greater than or equal to 20% of the total square footage of the historic portion of the property;

3) Paving or landscaping costs that exceed 10% of the total qualified expenditure;

4) Sales and marketing costs; or,

5) Expenditures not properly charged to a capital account, or, in the case of owner-occupied property, would not be charged to a capital account if the owner were using such property in a trade or business.

3. Estimated Revenue Loss[8]
   FY 19: $1.7 - $1.9 million
   FY 20: $1.2 - $1.6 million

4. Assessment
   For a more complete discussion, refer to analysis in Section 1.15

5. Inadvertent Effects
   Refer to analysis in Section 1.15.

2.12 Headquarters Management Company

1. Statutory Provision
   Title 30, Delaware Code, Chapter 64 and Chapter 20, §§2061 – 2064.

2. Description
   Headquarters Management Corporations (HMC's) are entities treated as a corporation under the Internal Revenue Code of the United States (Title 26 of the United States Code) that:

   a. Make an election to be taxed as a Headquarters Management Corporation; and

   b. The activities of which in this state are certified by the Director of Revenue to be confined to investment activities and/or the provision of headquarters services to itself and members of its affiliated group.

   Headquarters services include accounts receivable and payable; employee benefit plan administration; insurance; legal; payroll; data processing; purchasing; and tax, financial and securities accounting, reporting and compliance services provided by a Headquarters Management Corporation to itself and members of its affiliated group, and the maintenance and management of the intangible investments of other members of its affiliated group.

   HMC's were developed as a complement to Delaware Investment Holding Companies (See Item 2.01). Whereas even the most ardent supporters of

[8] These figures reflect the loss to the Corporate Income Tax only. With the exception of credits owned by individuals (see section 1.16), it appears that most of the remaining Historic Preservation Credits are owned by financial institutions. As such, there are millions of dollars in credits available that could offset Bank Franchise Tax liabilities. Given the transferability of these credits, at any time the credits may be conveyed to corporate taxpayers and then used to immediately reduce corporate income tax liabilities.

Investment Holding Companies would admit that they provide little in the way of direct employment benefits, HMC's were designed with the goal of increasing employment in Delaware for firms which limit their activities in Delaware to providing certain services to entities within their affiliated group.

HMC's are entitled to generous tax credits, which, by adding as few as five employees, eliminate 99% of the corporate income tax otherwise due. These credits are available for ten years.

3. Estimated Revenue Loss
FY 19: $0
FY 20: $0

4. Assessment
HMC's were established in 2004. Since that time, fewer than twenty HMC applications have been approved. As is the case with Investment Holding Companies, there is a high likelihood that the HMC's would not have been formed were not for 99% tax exemption offered under this provision. The fact that in fifteen-years' time so few firms have opted to take advantage of the HMC statute calls into question its general effectiveness as an economic development incentive.

5. Inadvertent Effects
None noted.

2.13 Asset Management Corporation

1. Statutory Provision
Title 30, Delaware Code, Chapter 19, §1903(b)(7).

2. Description
Asset Management Corporations (AMC's) are corporations that derive 90% or more of their federally-reported gross receipts from asset management services. Asset management services include, with respect to intangible investments:
   a. Rendering investment advice, including investment analysis;
   b. Making determinations as to when sales and purchases are to be made;
   c. Selling or purchasing;
   d. Rendering administration services;
   e. Rendering distribution services; or,
   f. Managing contracts for sub-advisory services.

Rather than the three-factor apportionment used by other corporations, asset management corporations are entitled to use customer-based sourcing and single factor, receipts-based apportionment.

3. Estimated Revenue Loss
FY 19: Negligible[9]
FY 20: Negligible

4. Assessment
The legislation establishing asset management corporations was adopted in response to evolving business practices within the financial services industry. In the mutual fund industry, for example, firms are increasingly engaging in related activities, such as pension fund management, that would fall outside of the scope of Delaware's mutual fund exemption. Because Delaware's mutual fund exemption is an "all or nothing proposition" (to qualify, 100% of a firm's activities must be confined to the management of intangible investments of mutual funds) any activity outside this scope, no matter how small, results in the loss of the exemption.

This provision is designed to allow firms the flexibility to engage in a wider array of financial activities without risking the loss of their tax advantaged status. The asset management corporation legislation was effective starting in tax year 2009. At present, fewer than five corporations have elected AMC status.

It is likely that any firms which are located in Delaware due to this distinction would not be located here in the absence of this preference. Therefore, the state would not likely stand to gain additional revenue if it were to eliminate the credit.

5. Inadvertent Effects
None noted.

2.14 Business Finder's Fee Tax Credit

1. Statutory Provision
Title 30, Delaware Code, Chapter 20, §§2090 – 2097.

[9] Accounts for likelihood of sweeping behavioral affect. See Assessment.

2. Description
This tax credit's purpose is to create incentives for existing businesses to partner with the state in the effort to create new employment opportunities for Delaware citizens, and to stimulate the Delaware economy by expanding the tax base. A finder's fee, a tool used commonly by businesses, is an arrangement by which an intermediary finds, introduces, and brings together parties to a business opportunity.

This provision rewards each Sponsor Firm (the "finder") and each New Business Firm (the business which relocates to Delaware) with a $500 annual tax credit per Delaware job created by the new business. The tax credit is available for three years. The program requires that the new business relocate to Delaware as a result of the efforts of the sponsor, and excludes those businesses, such as real estate agents, banks and commercial landlords, that already have an incentive to bring out-of-state business to Delaware.

3. Estimated Revenue Loss
FY 19: $0
FY 20: $0

4. Assessment
This provision became effective on October 1, 2010. Since its introduction, no businesses have applied for the Business Finder's Fee program.

5. Inadvertent Effects
Like all economic development tax incentives, there is a good chance that some of the firms that eventually take advantage of this legislation would have located in Delaware in its absence. In such cases, this legislation would act as a "bonus" instead of an incentive.

2.15 Veterans' Opportunity Credit

1. Statutory Provision
Title 30, Delaware Code, Chapter 20A, §§20A-100 – 20A-104.

2. Description
This preference provides an incentive for employers to hire veterans who fought in the War in Afghanistan or the Iraq War. Employers may claim a refundable credit against the bank franchise tax, corporate income tax, personal income tax, or insurance income tax equal to 10% of gross wages or

$1,500, whichever is lower, for each veteran they hire. Credits may be claimed in the year the veteran is hired and for two subsequent years.

This credit sunset on December 31st, 2015, however this assessment is included as credits generated in tax year 2015 could still be claimed through tax year 2017 (FY 2018 or 2019).

3. Estimated Revenue Loss
FY 19: $0
FY 20: Not Applicable

4. Assessment
Encouraging businesses to hire war veterans is a commendable goal. At least among employers subject to the corporate or personal income taxes, this credit appears to have provided little incentive to hire combat veterans.[10]

5. Inadvertent Effects
None noted.

2.16 Exemption of Out-of-State Resources During Declared Emergencies

1. Statutory Provision
Title 30, Delaware Code, Chapter 31, §§3101 – 3105.

2. Description
Delaware does not consider equipment and personnel employed during a declared state of emergency by infrastructure companies based in other states to constitute legal presence in the state for tax purposes if those assets are employed in emergency related work.

3. Estimated Revenue Loss
FY 19: Negligible
FY 20: Negligible

4. Assessment
This preference may facilitate the response to future disasters by eliminating tax concerns of companies employing out-of-state resources. During a declared emergency period, Delaware does not consider out-of-state businesses, workers, and property to have legal presence in this state of tax

[10] The credit may also be taken against the bank franchise and insurance premiums taxes, which may have experienced different rates of use than experienced under the personal and corporate income taxes.

purposes. Companies without prior nexus in the state will benefit from this preference as they will not have to file a corporate income tax return. Companies with prior nexus in the state will also benefit from this preference as they will not be required to consider out-of-state, emergency-related property and personnel in their apportionment formula.

The revenue lost from this preference is likely to be $0 for two reasons. First, the probability of a declared disaster occurring during any given fiscal year is small and unpredictable. Second, enforcement would likely be low if Delaware chose to tax this activity.

5. Inadvertent Effects
None noted.

2.17 New Economy Jobs Credit

1. Statutory Provision
Title 30, Delaware Code, Chapter 20, §§2080 – 2086.

2. Description
The purpose of this provision is to incentivize the creation of new, well-paying positions without regard to industry or occupation. Targeted economic incentives are frequently criticized as government's attempt to "pick winners" by singling out a specific industry for tax preferences or direct assistance. Instead, the logic behind this provision is that, in the long-run, labor markets will determine which skills and industries are most in demand. As such, the most effective incentive is one that implicitly accepts those results without limiting the incentive to a predetermined list of preferred activities.

During the 148th General Assembly, this credit expanded to include a benefit for retained jobs. A company involved in or resulting from a recent corporate restructuring which has its principal executive offices in Delaware and is focused on specific industries such as agricultural science, nutrition, biosciences, and safety may be eligible for a job retention credit. A program focused on job retention is founded on differing logic than one which targets new employment. Such a credit should be sufficiently narrow to continue to allow market forces to direct employment away from declining industries while still allowing the State to compete for retention of large employers in healthy industries considering leaving the State.

To qualify, a new employer must add at least 50 net new jobs with average annual salaries of at least $119,240 for tax year 2020.[11] This provision awards a refundable tax credit ranging from 25% to 40% of the qualified withholding taxes collected and paid on behalf of these new, qualified employees during the taxable year. Additional geographic-based credits are available to businesses that locate qualifying employees within targeted growth zones, incorporated municipalities, former brownfields and targeted growth counties.

The maximum aggregate credit is 65% of qualified withholding. Qualifying firms are eligible for credits over a ten year period. Eligibility in each year during that period is independently determined for new cohorts of employees.

Legislation enacted during the 147th General Assembly added additional ways a firm may qualify for this credit. Employers that create at least 200 jobs with an average salary of $70,000 (not indexed for inflation) in Delaware will be entitled to a tax credit equal to 25% of the withholding paid by the employer for the new jobs. If employers create more than 200 jobs, the size of the tax credit increases and can reach 40% if the employer creates 500 or more new jobs.

For retained jobs, the certified employer must maintain 200 jobs with an average salary of $70,000 in Delaware to earn a tax credit equal to 25% of the withholding paid by the employer on behalf of the retained employees. If employers retain more than 200 jobs, the size of the tax credit increases and can reach 40% if the employer retains 500 or more employees.

3. Estimated Revenue Loss
FY 19: $0
FY 20: $0

4. Assessment
This credit provides the Delaware Economic Development Office with a tool to recruit high-paying jobs to Delaware. Since its inception in 2007, no firms have made use of this credit. The possibility that this provision might go unused for several years is expected, because it is designed to help Delaware capitalize on rare, significant economic development opportunities, such as the potential relocation of a corporate headquarters.

[11] This salary threshold is adjusted for inflation (CPI growth) annually.

5. Inadvertent Effects
Like all economic development tax incentives, there is a good chance that some of the firms that take advantage of this legislation would have located or stayed in Delaware in its absence. In such cases, this legislation would act as a "bonus" instead of an incentive.

2.18 Vocational Rehabilitation Hiring Credit

1. Statutory Provision
Title 30, Delaware Code, Chapter 20B, §§20B-100 –20B-104.

2. Description
This preference provides an incentive for employers to hire individuals with a state-certified physical or mental disability who are in the process of, or have completed, vocational rehabilitative services. Employers may claim a refundable credit against the bank franchise tax, corporate income tax, personal income tax, or insurance income tax equal to 10% of gross wages or $1,500, whichever is less, for each qualified disabled worker they hire. Credits may be claimed in the year the qualified disabled worker is hired and for two subsequent years.

3. Estimated Revenue Loss
FY 19: $0
FY 20: Negligible

4. Assessment
The credit is available for employees hired on or after January 1st, 2017 and may be taken in the year of the hiring and up to two years thereafter. The tax credit can provide a labor market advantage for individuals with a qualified disability to offset other employment disadvantages they might have faced.

5. Inadvertent Effects
Refer to Section 1.18.

2.19 Apportionment Election Preference for Worldwide Headquarters and Telecommunication Companies

1. Statutory Provision
Title 30, Delaware Code, Chapter 19, §§1901 – 1903.

2. Description

As part of legislation enacted in the 148th General Assembly to modernize Delaware's apportionment of multi-state firms' profits—moving from three factor apportionment to single sales factor apportionment over a five year period—Telecommunications Corporations (TCCs) and Worldwide Headquarters Corporations (WHCs) are allowed to annually elect their apportionment method between equally weighted three factors or a single sales factor beginning in tax year 2017.

TCCs are members "of a group of corporate and non-corporate entities, which group (a) consists of corporate and non-corporate entities that are affiliated through relationships described in § 267(b) of the Internal Revenue Code, (b) provides both intrastate mobile telecommunications services and other intrastate telephone services, as such terms are used in § 5501(8)a.3. of [Title 30], and (c) in the aggregate earns annual gross receipts in the United States from providing intrastate and interstate telephone and telecommunications services, and from providing Internet access, as such term is defined in § 5501(6) of [Title 30], in excess of" $50 billion.

WHCs are corporations that (a) list the site of their principal executive offices as an address in Delaware in their From 10-Q filing with the SEC for the quarter immediately prior to January 1st, 2017, (b) employ at least 400 full-time employees at the corporate headquarters in Delaware as of January 1st, 2016, and (c) make or contract for a capital investment of not less than $25 million to renovate or improve the corporate headquarters in Delaware between July 1st, 2014 and June 30th 2018.

3. Estimated Revenue Loss

FY 19: (D)
FY 20: (D)

(D) = Per 30 Del. C. §368, the Department of Finance is prohibited from disclosing tax return information identifying specific taxpayers.

4. Assessment

At the time of enactment, the full impact of the Delaware Competes Act was projected to cost $8.2 million in FY 17 and $17.6 million in FY 18 for all corporate income taxpayers in Delaware. The costs associated with the TCC and WHC provisions are likely to be a very small portion of those estimated costs.

The WHC provisions may be attractive for a few large Delaware-based firms with the potential for growth. Single-sales factor apportionment removes any negative tax consequences for expanding property and payroll in the State. Accordingly, there is no need for WHCs to defer expansion decisions until 2020.

Because TCCs are less likely to have large property and payroll shares in Delaware, this incentive may have less significance for them. Should TCCs continue to utilize three factor apportionment, then the cost of the TCC preference will continue beyond the end of the single-sales apportionment phase-in.

5. Inadvertent Effects

Providing a preference for firms in one sector of the economy may create an incentive for other firms to recharacterize their activities in such a way that they meet the legal requirements for eligibility. While the strict definitions and high barriers to entry in telecommunications industries likely prevent this issue, it is possible that some firms may be able to do so and create a basis for claiming the single-sales apportionment. To the extent they are successful, the cost of this provision rises with no benefit in terms of Delaware employment or property ownership. Such preferences may also increase administrative costs related to enforcing narrowly defined eligibility standards.

2.20 Automatic External Defibrillator Tax Credit

1. Statutory Provision

Title 30, Delaware Code, Chapter 20C, §§20C-100 – 20C-101.

2. Description

This preference provides an incentive for employers to place into service automatic external defibrillators (AED) at business locations within the State of Delaware. For each AED placed into service after December 31, 2017, the taxpayer is entitled to a one-time credit of $100.

3. Estimated Revenue Loss
   FY 19: Negligible
   FY 20: Negligible

4. Assessment
   This credit is intended to incentivize private businesses in Delaware to install potentially life-saving devices at their location. The Delaware Department of Health, Office of Emergency Medical Services provides free AED devices through the Delaware Early Defibrillation Program. The $100 credit may not be likely to incentivize the purchase of a device, which typically cost between $1,200 and $3,000. Because this incentive is a credit against taxes due, entities without a tax liability (e.g. non-profits) would not benefit from this preference.

5. Inadvertent Effects
   None noted.

MOTOR FUEL/SPECIAL FUEL TAX

- Statutory Provision

  Title 30, Delaware Code, Chapter 51.

- Collection/Administrative Agency

  The Department of Transportation, Motor Fuel Tax Administration, administers this tax.

- General Liability

  Delaware imposes an excise tax on each gallon of gasoline sold or used in the state. The tax is collected by and paid to the state by licensed distributors. An excise tax is also imposed on the retail sale or use of special fuel, which includes all combustible gases and liquids suitable for propulsion of motor vehicles except fuels that are determined to be gasoline or gasohol. The special fuel tax is collected by and paid to the state by licensed suppliers, users, and dealers. A new excise tax is imposed for certain aviation jet fuel designed for use in the operation of jet or turbo-prop aircraft, effective July 1, 2019.

- Tax Rates

  The excise tax rate is 23 cents per gallon of gasoline, 22 cents per gallon of special fuel, or 5 cents per gallon of aviation jet fuel, sold or used in the state.

- Tax Receipts ($ millions)[1]

Fiscal Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total ($)	112.9	113.8	112.9	112.6	113.6	117.0	124.6	129.5	131.6	142.8

- Tax Preferences

  The following table identifies motor and special fuel tax preferences within the Delaware Code along with annual estimated costs. Links within the table navigate to more detailed analysis of each tax preference.

[1] Figures are for gasoline and special fuel receipts

TAX PREFERENCE	FY 19 (EST)	FY 20 (EST)
3.01 Motor Fuel Tax Exemptions	$12,000	$12,000
3.02 Motor Fuel Tax Refunds	$60,000	$60,000
3.03 Special Fuel Exemptions	$45,000	$45,000
3.04 Aviation Jet Fuel Exemptions	N/A	Unknown

3.01 Motor Fuel Tax Exemptions

1. Statutory Provision
   Title 30, Delaware Code, Chapter 51, Subchapter I, §5111(a)(5).

2. Description
   This provision exempts gasoline sold to volunteer fire companies, veterans' groups, and civic ambulance companies from the motor fuel tax.
   Section 5111 of the Delaware Code also exempts gasoline sold to the federal or state government from the motor fuel tax. However, these exemptions for governments are not considered tax preferences for the purpose of this report. (Please see section titled "Delaware Tax Provisions Not Included" for more discussion.)

3. Estimated Revenue Loss
   FY 19: $12,000
   FY 20: $12,000

4. Assessment
   Whether the tax code is the most appropriate policy tool to provide public support for these activities is open to question. Proponents of the preference may argue that the exemption is justified because these organizations perform quasi-public service functions that the state or one of its political subdivisions would otherwise provide.

5. Inadvertent Effects
   None noted.

3.02 Motor Fuel Tax Refunds

1. Statutory Provision
   Title 30, Delaware Code, Chapter 51, Subchapter I, §5120(a).

2. Description
This provision allows for a refund of motor fuel taxes in the following circumstances:

- Gas sold for use in stationary engines, tractors, motor boats, aircraft, and any other vehicle or machine that does not utilize public highways; or,

- Gas sold to operators of a taxicab business with a base of operations in Delaware.

3. Estimated Revenue Loss
FY 19: $60,000
FY 20: $60,000

4. Assessment
Because the motor fuel excise tax is intended to be a road use tax, the exemption of fuel in off-highway vehicles and machines is considered legitimate. However, one may question the exemption for taxicabs, as their operation undoubtedly occurs on public roads and highways. Additionally, with the rise of ride-sharing services, the equity of this preference for taxicabs is further brought into question.

5. Inadvertent Effects
None noted.

3.03 Special Fuel Exemptions

1. Statutory Provision
Title 30, Delaware Code, Chapter 51, §5133(a).

2. Description
This provision exempts special fuels—primarily diesel—sold to volunteer fire companies, veterans' groups, and civic ambulance companies from the special fuel tax.

Section 5111 of the Delaware Code also exempts fuel sold to the federal or state government from the special fuel tax. However, these exemptions for governments are not considered tax preferences for the purpose of this report. (Please see section titled "Delaware Tax Provisions Not Included" for more discussion.)

3. Estimated Revenue Loss
FY 19: $45,000
FY 20: $45,000

4. Assessment
The rationale for exempting special fuels used by eligible vehicles is consistent with the exemption of such vehicles from the motor fuels tax. Please refer to the discussion in Items 3.01 and 3.02.

5. Inadvertent Effects
None noted.

3.04 Aviation Jet Fuel Exemptions

2. Statutory Provision
Title 30, Delaware Code, Chapter 51, §5172(b).

3. Description
This provision exempts aviation jet fuels used for aerial application within the State from the aviation jet fuel tax. It also exempts, for a temporary period not to exceed 5 years, aviation jet fuel used for the purpose of economic development and job creation in the aviation industry in the State. This exemption must be approved by the Council on Development Finance and the Director of Small Business.

Section 5172 of the Delaware Code also exempts fuel sold to the federal or state government from the aviation jet fuel tax. However, these exemptions for governments are not considered tax preferences for the purpose of this report. (Please see section titled "Delaware Tax Provisions Not Included" for more discussion.)

4. Estimated Revenue Loss
FY 19: N/A
FY 20: Unknown

5. Assessment
Aviation jet fuel used for aerial application, which is spraying crops with crop protection products from an agricultural aircraft, is a business input in the agricultural process, not a final product. Taxing business inputs violates several tax policy principles and causes economic distortions.

6. Inadvertent Effects
None noted.

PUBLIC UTILITY TAX

- Statutory Provision

  Title 30, Delaware Code, Chapters 33, 41 and 55.

- Collection/Administrative Agency

  The Department of Finance, Division of Revenue, administers this tax.

- General Liability

  Firms that provide steam, gas, electric, telephone, telegraph, or cable television services are subject to the public utility tax. Except for cable television services, receipts from sales to residential users are exempt from this tax. A separate license tax is based on gross receipts of businesses that produce steam, gas, or electricity.

- Tax Rates

UTILITY	TAX RATE	PAYMENT DATES
Electricity Distribution	4.25% of gross receipts from non-residential users. 2.0% of gross receipts from manufacturers, food processors and agribusinesses. Sales to automobile and certain other types of manufacturers are exempt.	Returns and payment due on or before the 20th day after the end of each calendar month.
Gas Distribution	4.25% of gross receipts from non-residential users. 2.0% of gross receipts from manufacturers, food processors and agribusinesses. Sales to automobile manufacturers are exempt.	Returns and payment due on or before the 20th day after the end of each calendar month.
Intrastate Telephone & Telegraph Services	5.0% of gross receipts from non-residential users	Returns and payment due on or before the 20th day after the end of each calendar month.
Cable and Satellite Television Distribution	2.125% of gross receipts	Returns and payment due on or before the 20th day after the end of each calendar month.
Electricity and Gas Manufacturing and Production	0.1 % (one mill) on each dollar of gross receipts from the production of gas or electricity. Municipalities are exempt.	Returns and payments are due on the first Monday of May.

- Tax Receipts (millions of dollars)

Fiscal Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Total ($)	56.7	57.2	45.4	44.5	47.4	47.2	45.0	43.7	43.1	37.0

- Tax Preferences

The following table identifies public utility tax preferences within the Delaware Code along with annual estimated costs. Links within the table navigate to more detailed analysis of each tax preference.

TAX PREFERENCE	FY 19 (EST)	FY 20 (EST)
4.01 Public Utility Exemption for Corporations Reorganizing Under Provisions of the Bankruptcy Code	Negligible	Negligible
4.02 Exemption of Electricity Used in Certain Manufacturing Processes	$175,000	$100,000 - $200,000
4.03 Refunds of Public Utility Tax to Firms That Qualify for the New Facilities Business Credit Program	Negligible	Negligible
4.04 Rate Reduction for Electricity Used by Manufacturing, Agribusiness and Food Processing Firms	$1.1m	$1.0-$1.25m
4.05 Rate Reduction for Gas Used by Manufacturing, Agribusiness and Food Processing Firms	$170k	$150-$250k
4.06 Exemption of Electricity Used By Automobile Manufacturers	$0	$0
4.07 Exemption of Gas Used By Automobile Manufacturers	$0	$0
4.08 Rate Reduction for the Provision of Cable and Satellite Television Services	$10.1m	$10.0-$10.5m
4.09 Exemption for Electronic Pager Service	Negligible	Negligible

4.01 Public Utility Exemption for Corporations Reorganizing Under Provisions of the Bankruptcy Code

1. Statutory Provision
   Title 30, Delaware Code, Chapter 55, §5506(f).

2. Description
   The public utility tax on gas and electricity is exempted for 36 consecutive months for any corporation which is a debtor in possession in a reorganization proceeding under Chapter 11 of the United States Bankruptcy Code.

3. Estimated Revenue Loss
   FY 19: Negligible
   FY 20: Negligible

4. Assessment
   This exemption is intended to assist ailing Delaware firms that are considered extremely important to the state economy. This exemption could result in a significant revenue loss if given to one or more firms that are a large electricity consumer. No firms are known to have claimed this exemption over the course of the last several years, and none are expected to do so in the near future.

5. Inadvertent Effects
   None noted.

4.02 Exemption of Electricity Used in Certain Manufacturing Processes

1. Statutory Provision
   Title 30, Delaware Code, Chapter 55, §5506(g).

2. Description
   Gross receipts from electricity used in electrolytic (decomposition of a chemical compounds using an electrical current), electroarcthermal (steel production using electric arcs for heating), or air separation manufacturing processes (separation of air into its component parts by electric charge) are exempt from the public utility tax.

3. Estimated Revenue Loss
   FY 19: $175,000
   FY 20: $100,000 - $200,000

4. Assessment
This preference attempts to strengthen the competitive position of certain Delaware manufacturers relative to neighboring states by assisting specific types of firms that use large amounts of electricity in production. How successfully this tax preference meets its objective is unknown.

5. Inadvertent effects
None noted.

4.03 Refunds of Public Utility Tax to Firms That Qualify for the New Facilities Business Credit Program

1. Statutory Provision
Title 30, Delaware Code, Chapter 55, §5507.

2. Description
Any firm that is eligible for New Job Creation Credits (defined under Title 30, Section 2011(a), formerly Blue Collar Jobs Credits) is also entitled to receive for five years a rebate of 50 percent of the public utility tax that it owes on the operation of new or expanded enterprises.

3. Estimated Revenue Loss [1]
FY 19: Negligible
FY 20: Negligible

4. Assessment
This program was implemented as a component of the Blue Collar Jobs Act in order to enhance the business climate for the state's manufacturers. For a full discussion, please refer to Item 2.05, 2.06, 2.08 and 2.09 in the corporate income tax section of this report.

5. Inadvertent effects
None noted.

[1] This estimate can vary significantly from year to year as claims for refunds from a handful of major energy-using firms can widely change the total amount of refunds.

4.04 Rate Reduction for Electricity Used by Manufacturing, Agribusiness and Food Processing Firms

1. Statutory Provision
   Title 30, Delaware Code, Chapter 55, §5502(b)(2).

2. Description
   This provision lowers the tax rate for all manufacturers in the state who do not qualify for the electrochemical manufacturing exemption discussed above (see Item 4.02). The public utility tax on electricity sold to Delaware manufacturers is 2 percent, as opposed to the general 4.25 percent rate.

3. Estimated Revenue Loss
   FY 19: $1.1 million
   FY 20: $1.0 - $1.25 million

4. Assessment
   This preference attempts to strengthen the competitive position of Delaware's manufacturers relative to neighboring states by assisting firms that use large amounts of electricity in production. How successful this tax preference is in its purpose is unknown. For firms using significant amounts of electricity in the production process, overall power rates may be much more important than the 2.25 percentage point reduction provided by this provision in determining whether the state's utility rates are affordable and competitive. While this provision provides a 53 percent reduction in tax rates, the overall reduction in electricity costs is only 2.16 percent. For example, consider a firm that spends $10,000 annually on electricity. The savings provided by this provision are calculated as follows:

Cost Savings from Utility Rate Reduction		
Amount spent on electricity (before taxes):	**$10,000**	
Amount spent on electricity under 4.25% rate:	**$10,425**	($10,000 * 1.0435)
Amount spent on electricity under 2.0% rate:	**$10,200**	($10,000 * 1.02)
Difference	**$225**	($10,425 - $10,200)
Percent reduction:	**2.16%**	($225 / $10,425)

A flaw of broad, industry-based preferences such as this is that firms obtain tax relief solely because they fall under a definition of "manufacturing." Firms in other industries may actually be larger power users or in more competitively precarious positions but do not meet the statutory definition.

5. Inadvertent effects
Enacting a public utility tax preference for a single sector of the economy may cause firms in that industry to lag in the introduction of more energy-efficient production technologies. Given the relatively small benefit provided by this preference, however, this outcome seems unlikely.

Additionally, providing a preference for firms in one sector of the economy may create an incentive for other firms to construe their activities in such a way that they meet the legal requirements for eligibility. For some firms, non-substantive changes to their activities or accounting practices can create a basis for claiming entitlement to benefits. To the extent that they are successful, the cost of this provision is increased with no concomitant increase in benefits. Such preferences may also increase administrative costs in enforcing narrowly defined eligibility standards.

4.05 Rate Reduction for Natural Gas Used by Manufacturing, Agribusiness and Food Processing Firms

1. Statutory Provision
Title 30, Delaware Code, Section §5502(b)(2).

2. Description
This provision reduces the public utility tax rate on receipts from natural gas consumed by manufacturers, agribusinesses and food processing firms to 2.0%. The general rate is 4.25%

3. Estimated Revenue Loss
FY 19: $170,000
FY 20: $150,000 - $250,000

4. Assessment
Generally speaking, the same assessment of the rate reduction for receipts from electricity consumed by manufacturers (item 4.04) can be applied to this preference. However, an evaluation of this preference must also take into account that a rate preference for electricity consumed by manufacturers existed for several years prior to the enactment of this provision. As such, a rate differential existed between electricity and gas used in manufacturing processes. To the extent that these inputs could be substituted, manufacturers had a tax induced incentive to favor electricity over natural gas. By eliminating the rate differential, the economic decisions of manufacturers for inputs in the production process will be less distorted by tax code provisions.

5. Inadvertent effects
See item 4.04.

4.06 Exemption of Electricity Used By Automobile Manufacturers

1. Statutory Provision
Title 30, Delaware Code, Chapter 55, §5506(j).

2. Description
This provision exempts automobile manufacturers from paying the public utility tax on electricity that they use in vehicle production.

3. Estimated Revenue Loss
FY 19: $0
FY 20: $0

4. Assessment
Noting the large "multiplier effect" that automobile plants had on Delaware's economy, the General Assembly added this provision in the spring of 1995. Automobile Manufacturers were then critical Delaware employers. While this provision likely provided only a minor benefit to auto manufacturers, it demonstrates a visible commitment by the state to this sector of the economy.

Ultimately, in the wake of the closure of the state's two auto plants, relative to the powerful economic and operational challenges that faced Delaware's auto industry, this preference's relief proved irrelevant.

5. Inadvertent effects
Enacting a public utility tax preference for a single sector of the economy may cause firms in that industry to lag in the introduction of more energy-efficient production technologies. Given the relatively small benefit provided by this preference, however, this outcome seems unlikely.

4.07 Exemption of Natural Gas Used By Automobile Manufacturers

1. Statutory Provision
Title 30, Delaware Code, Chapter 55, §5506(j).

2. Description
This provision exempts automobile manufacturers from paying the public utility tax on natural gas that they use in vehicle production.

3. Estimated Revenue Loss
FY 19: $0
FY 20: $0

4. Assessment
Generally speaking, the same assessment of the exemption for receipts from electricity consumed by automobile manufacturers (item 4.06) can be applied to this preference. However, an evaluation of this preference must also take into account that an exemption for electricity consumed by automobile manufacturers existed for several years prior to the enactment of this provision. As such, a rate differential existed between electricity and gas used in this manufacturing process. To the extent that these inputs could be substituted, manufacturers had a tax induced incentive to favor electricity in the production of automobiles over natural gas. By eliminating the rate differential, the economic decisions of automobile manufacturers for inputs in the production process will be less distorted by tax code provisions.

Ultimately, in the wake of the closure of the state's two auto plants, relative to the powerful economic and operational challenges that faced Delaware's auto industry, this preference's relief proved irrelevant.

5. Inadvertent effects
See Item 4.06

4.08 Rate Reduction for the Provision of Cable and Satellite Television Services

1. Statutory Provision
Title 30, Delaware Code, Chapter 55, §5502(b)(4).

2. Description
This preference imposes a reduced rate of 2.125% (as opposed to 5.00% for other telecommunication services) on the provision of cable and satellite television communications, commodities and services. The legal incidence of this tax falls on entities distributing cable television services within the state of Delaware.

3. Estimated Revenue Loss
FY 19: $10.1 million
FY 20: $10.0 - $10.5 million

4. Assessment
Although it can be debated whether this provision is appropriately included in this report, it is treated as a tax preference because it taxes one type of public utility service differently from others and it meets the definition of a tax preference found in 8305(6) of Title 29.[2] As this report is meant to be as inclusive as possible, an argument can be made to include this item.

The goal of this preference appears to be the provision of tax relief to residential consumers. Unlike most other elements of the public utility tax, which are limited to nonresidential services, the tax on cable and satellite services applies to residential and nonresidential consumption. By applying a lower tax rate to these services, this provision achieves this goal.

5. Inadvertent effects
None noted.

4.09 Exemption for Electronic Pager Service

1. Statutory Provision
Title 30, Delaware Code, Chapter 55, §5501(7)(b).

2. Description
This provision excludes electronic pager service from the public utility tax.

3. Estimated Revenue Loss
FY 19: Negligible
FY 20: Negligible

4. Assessment
This exemption differentiates electronic pager service from other types of telecommunications service. Traditional electronic pagers have limited functionality and advances in telecommunications technology have essentially rendered pagers obsolete. With the advent of smart phones, which provide a wider array of services, it is increasingly clear that "stand-alone" pagers are becoming a technological anachronism, calling into question the policy rationale for continuing this preference.

[2] The definition of a "tax preference" found in §8305(6) describes a preference as a tax code provision that (among other things) "...exempts, in whole or in part, certain persons, income, goods, *services* or property from the impact of established taxes..." The federal definition speaks more directly to the issue by defining a tax preference as "a preferential rate of tax."

5. Inadvertent effects
   None Noted.