Federal Tax Reform

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Two Levels of Income Taxes Impacted

Federal Tax Reform

Impact on Utahans

FEDERAL Income Tax Liability
- Individuals
- Businesses

STATE Income Tax Liability
- Individuals
- Businesses
Key Changes to **Federal Individual Income Tax**

Note that Most changes begin in 2018 and expire after 2025
Key Changes to Federal Individual Income Tax

Generally:
• Rates go
• Bracket thresholds go

<table>
<thead>
<tr>
<th>Rate</th>
<th>Bracket Thresholds*</th>
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<tr>
<td>10%</td>
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<tr>
<td>15%-12%</td>
<td>$19,050</td>
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<tr>
<td>25%-22%</td>
<td>$77,400</td>
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<tr>
<td>28%-24%</td>
<td>$156,150 - $165,000</td>
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<tr>
<td>33%-32%</td>
<td>$237,950 - $315,000</td>
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<tr>
<td>35%</td>
<td>$424,950 - $400,000</td>
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<tr>
<td>39.6%-37%</td>
<td>$480,050 - $600,000</td>
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</table>

*Bracket thresholds shown are for married taxpayers filing a joint return.
Key Changes to **Federal Individual** Income Tax

- Increases federal Adjusted Gross Income (AGI) by repealing deductions for:
  - Moving expenses
  - Alimony payments (2019)
- Decreases AGI by no longer counting alimony as income
- These are marginal changes

- AGI is the starting point for Utah’s individual income tax
Key Changes to **Federal Individual** Income Tax

- Repeals itemized deductions (casualty/theft losses; Job expenses)
- Limits mortgage interest deduction
  - New purchases ($1,000,000 → $750,000)
  - Eligible equity debt must be used to “buy, build, or substantially improve your home”
- Caps deductions for state and local taxes at $10,000
- Charitable deduction is largely kept the same
- Repeals the limit on total itemized deductions
Key Changes to Federal Individual Income Tax

• Nearly doubles the standard deduction ($13,000 → $24,000)
• Repeals personal exemptions ($4,050 → $0)
• Increases the child tax credit ($1,000 → $2,000)
  • $1,400 refundable (indexed)
  • Child must have SSN
• Creates a new $500 family tax credit for dependents ineligible for the child tax credit
Key Changes to **Federal Individual** Income Tax

- Expands use of 529 accounts (think UESP) to include K-12 education expenses
  - Includes expenses for private school and homeschool
  - Utah offers an income tax credit for contributions to a UESP 529 account
    - 2017 credit cap is $192 (indexed for inflation)
    - In 2016, 16,941 people claimed credits totaling $2.8 million
Key Changes to Federal Individual Income Tax

Traditional CPI vs. Chained CPI used to index brackets and credits
Key Changes to **Federal Individual Income Tax**

• What’s the impact on Utahans’ federal income tax liability?
  • Most people should see a tax cut
  • How much of a cut depends on a variety of factors
  • Online tax calculators
  • One group that is likely to face an increase: Upper middle income families that have dependents older than 17
    • Trade $4050 exemption for a $500 credit

• The IRS and State Tax Commission do not provide us with sufficient data to calculate total impacts for all Utahans
Key Changes to Federal Business Income Taxes
Key Changes to **Federal Business** Income Taxes

- 21% single-rate corporate income tax
- New 20% deduction for certain Pass-through entities
  - Based on Qualified Business Income (QBI)
  - Capped at 50% of pass-throughs’ employees’ W-2 wages
  - Deduction phases out beginning at $157k/$315k
  - Not sure if it will be considered an itemized deduction
  - Pass-through entities get the same rate reductions as individuals (see slide 4)
Key Changes to **Federal Business** Income Taxes

- Changes taxation of multinational entities from a worldwide system to a territorial system (anti-abuse rules)
- “Deemed repatriation” for income stashed over seas
  - All foreign profits are deemed to have been brought back to U.S. and immediately taxed
  - 15.5% rate on liquid assets
  - 8% rate on other assets
- Estimated $2.6 trillion in untaxed earnings over seas
- Raises $339 billion over 10 years
What were the drivers of federal tax reform?

Improve the International Competitiveness of the US Corporate Income Tax System

CIT Rate

Worldwide Taxation
Territorial Taxation

US Post-TCJA
Key Changes to Federal Business Income Taxes

• Modifies the Section 179 expensing election (small business)
  • Raises the depreciation cap ($500k–$1 million)
  • Increases phaseout threshold ($2 million–$2.5 million)

• Modifies bonus depreciation for business property
  • Acquired and placed in service after September 27, 2017
  • 50% 100% expensing through 2022
  • Phases down to 20% from 2023 to 2026
  • New and used property
Key Changes to **Federal Business** Income Taxes

- Caps the net interest deduction at 30% of adjusted taxable income
- Repeals corporate Alternative Minimum Tax (AMT)
- Changes treatment of Net Operating Loss (NOL)
  - **2-year No** carryback
  - **20-year Infinite** carryforward with 80% of taxable income limitation
- Utah has a limited 3 year carryback and a 15 year carryforward
Key Changes to Federal Business Income Taxes

• What’s the impact?
  • Most economist say it will provide a boost to the U.S. economy
    • Size and length of “boost” is debatable
    • Estimated average yearly increase in GDP growth over 10 years is between 0.05 and 0.12 percentage points
  • Businesses are expecting to see a big increase in profits
    • How will businesses spend the increased profits?
      • Jobs, capital expenditures, bonuses and raises, shareholders
  • Increase the deficit ($500 billion and $1.5 trillion over 10 years)
Bringing it Home

How Federal Tax Reform Impacts Utah
Individual Connections

Exemptions

AGI
Individual Connections

Federal Itemized or Standard Deduction Amount
Utah Taxpayer Tax Credit

• **Credit base** is 6% of the sum of **exemptions** and **deductions**
  • Exemptions: number of Utah exemptions times 75% of the federal personal exemption amount ($3,038 per Utah exemption)
  • Deductions:
    • (1) standard deduction ($6,300 for single filers and $12,600 for married filers); or
    • (2) itemized deductions less state and local income taxes deducted

• **Credit phaseout** is 1.3 cents per dollar of income in excess of:
  • Filing single/married filing separately, $13,867
  • Married filing jointly/qualifying widow(er), $27,734
Big Levers - Individual

• Impact on Utah Tax Liability/Revenue:
  • Elimination of **Personal Exemption**
  • Doubling of **Standard Deduction**
  • Limitations on **Itemized Deductions**
  • Increased Child/Family Tax Credit
Corporate Connections

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**U.S. Corporation Income Tax Return**

For calendar year 2016 or tax year beginning 2016, ending _______

INFORMATION ABOUT FORM 1120 AND ITS SEPARATE INSTRUCTIONS IS AT WWW.TREASURY.GOV/FORM1120

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<td>ZIP Code</td>
<td>Other</td>
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**Schedule A - Utah Net Taxable Income and Tax Calculation**

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<th>Description</th>
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**Taxable Income**
Orders of Magnitude on Corporate Education Fund

Delta (+/- $20m)
Other Business Connections...
New 20% deduction may be an Itemized or added to the Standard Deduction
...Or maybe not.
If Utah does not change its tax code . . .

<table>
<thead>
<tr>
<th>Implementation of New 20% Deduction</th>
<th>Estimated Additional State Dollars (millions)</th>
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<tr>
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<td>FY2019</td>
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<tr>
<td>No impact on itemized or standard deduction</td>
<td>$80</td>
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<td>Impacts itemized deduction only</td>
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<td>Impacts itemized and standard deduction</td>
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</table>
• There is still **a great deal of uncertainty** in these estimates due to unknown behavioral changes that will no doubt result from the new tax rules.

• Because of that uncertainty and our lack of detailed data on corporate taxes, we did not model corporate tax changes. We believe any downside risk on corporate revenue would be within the margin of error on our consensus estimates.
Policy Options

• Do nothing / Wait and see
• Try to mitigate impacts of federal tax reform now
  • State revenue as a whole
  • Tax liability of each taxpayer
• Use new revenue to offset cost of some other policy change