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TCJA Expiration & Potential Renewal: Impacts on the States

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What is the Tax Cuts & Jobs Act (TCJA)?

- TCJA was a business code reform and individual cuts together in the same bill, enacted 2017
- Business Code Reform
  - Rate Reduction from 35% to 21% - permanent
  - Territorial, including transition tax – permanent (and constitutional! *Moore*)
    - Anti-Abuse Provisions (GILTI, BEAT, FDII) & reduction of interest expense deduction
  - Expensing - 100% through 2022, then phases out 20% a year
- Individual Cuts – *all expire end of 2025*
  - Across-the-board rate cuts
  - Doubled standard deduction, SALT cap, mortgage interest deduction limit
  - Estate tax exemption doubled
  - AMT patch
  - Child tax credit ($1,000->$2,000->$3,000->$2,000->$1,000)
  - 199A

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TCJA Federal Revenue Impacts

- TCJA originally was designed as a $1.5 trillion net tax cut over 10 years
  - Revenue increases of $4 trillion
    - Capping individual deductions, eliminating personal exemptions ($1.9t)
    - Corporate mandatory repatriation tax ($0.8t one-time)
    - Corporate Anti-abuse provisions ($0.3t)
  - Revenue decreases of $5.5 trillion
    - Lower individual rates and doubled standard deduction ($1.9t)
    - Lower corporate rate and expensing ($1.4t)
    - AMT patch ($0.7t)
    - Child tax credit expansion ($0.5t)
    - 199A
    - Estate tax exemption level doubling
  - Proposed “border adjustment” VAT-like provision was dropped from GOP plan
  - Straight-line extension estimate: $4 trillion+ net reduction

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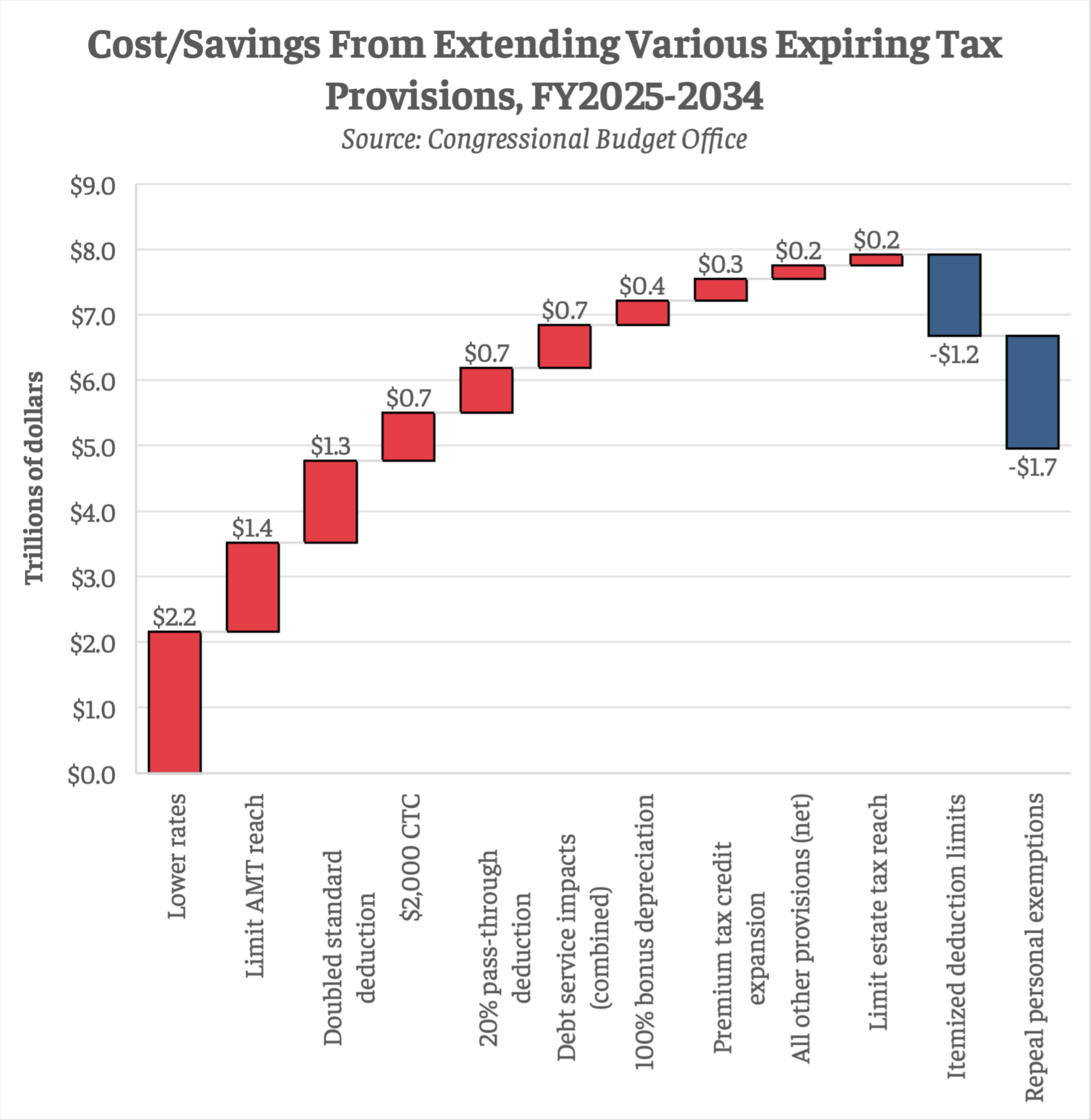
Cost/Savings From Extending Various Expiring Tax Provisions, FY2025-2034
Source: Congressional Budget Office
Trillions of dollars
$9.0
$8.0
$7.0
$6.0
$5.0
$4.0
$3.0
$2.0
$1.0
$0.0
$2.2
$1.4
$1.3
$0.7
$0.7
$0.7
$0.4
$0.3
$0.2
$0.2
-$1.2
-$1.7
Lower rates
Limit AMT reach
Doubled standard deduction
$2,000 CTC
20% pass-through deduction
Debt service impacts (combined)
100% bonus depreciation
Premium tax credit expansion
All other provisions (net)
Limit estate tax reach
Itemized deduction limits
Repeal personal exemptions

Other Tax Issues Likely to Come Up

- Promises/Statements by President-elect Trump
  - No tax on tips
  - No tax on overtime
  - No tax on Social Security benefits
  - Restore SALT deduction
  - Tariffs
- Other matters Congress will likely confront
  - Wyden-Smith bill (2024 passed House, died in Senate): expand Child Tax Credit, restore expensing, cut off Employee Retention Tax Credit (ERTC)
  - Energy credits in the Inflation Reduction Act (IRA)
  - Spending (DOGE), debt ceiling, FY 2025 budget
  - IRS funding
- International: Pillar 1 (transfer pricing rules for multinational digital companies) & Pillar 2 (global 15% corporate minimum tax)

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TCJA State Impacts

1. Impacts from Conformity
2. Impacts from Income Starting Point
3. Impacts from Standard Deduction
4. Impacts from Itemized Deduction Changes
5. Impacts from International and NOL Provisions
6. Impacts from Estate Tax changes
7. Impacts from Complexity changes
8. Impacts from Expensing
9. Total Impact
10. Predictions

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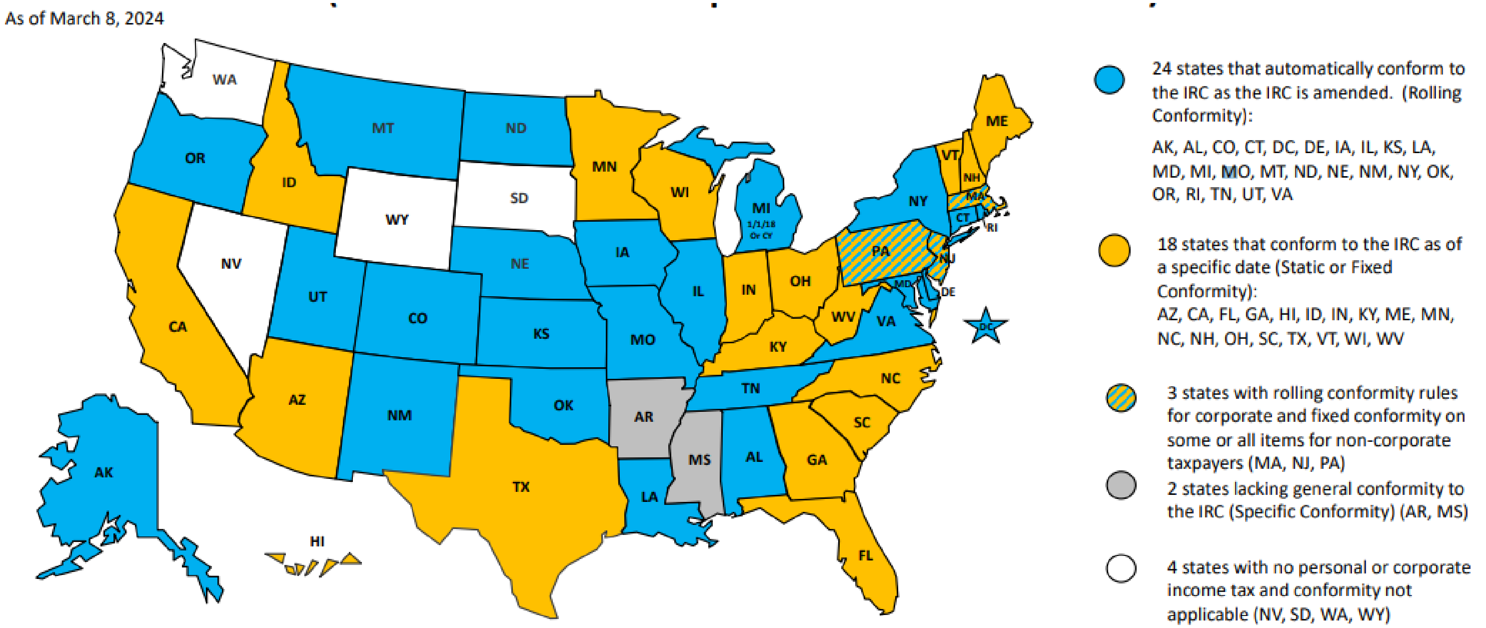
1. Impacts from Conformity

- 24 states automatically conform to the federal tax code (rolling conformity) & 18 states as of a certain date (static conformity)
  - TCJA in 2017 roughly expanded the base (which many states conform to) and cut rates (which most states do not conform to), so states generally saw more revenue from TCJA. The reverse will occur with expiration.



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2. Impacts from Income Starting Point

- 5 states impose state tax on the federal definition of taxable income
  - Colorado, Montana, New Mexico, North Dakota, South Carolina
  - Changes to the federal tax base directly changes the state tax base
- Most other states start from adjusted gross income
  - Some impose tax directly on AGI calculation (IL, IN, KY, MA, MI, UT)
  - Changes to the tax base generally flow through to the state tax base

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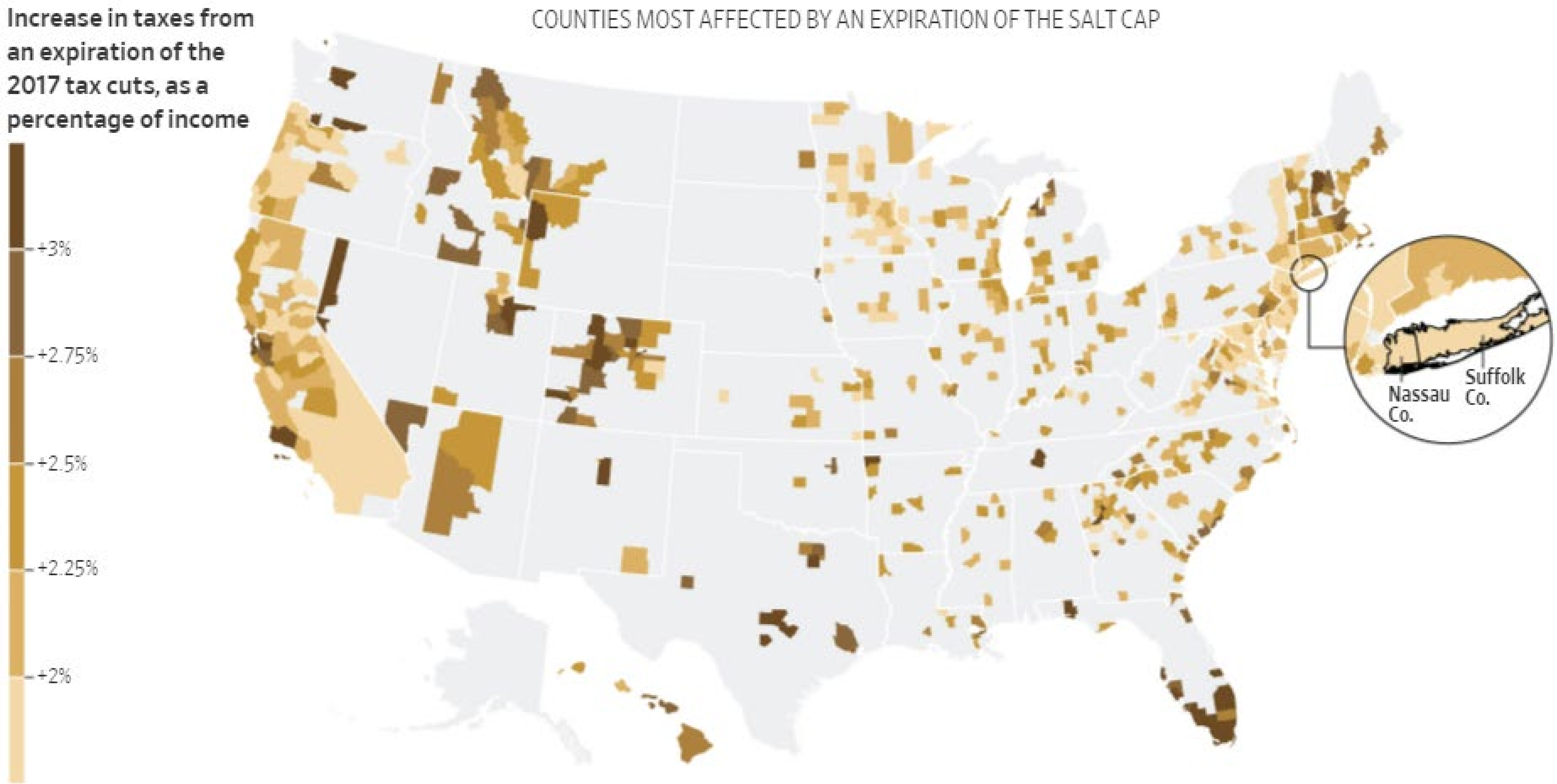
3. Impacts from Standard Deduction

- 9 states & DC adopt the federal standard deduction as theirs for state income tax purposes
  - Arizona, Colorado, Idaho, Maine, Missouri, Montana, New Mexico, North Dakota, South Carolina, and the District of Columbia.
  - Expiration of the federal expanded standard deduction would also mean a tax increase for taxpayers in those 9 states.
- Despite TCJA setting the personal exemption to $0, most states retain a personal exemption for state taxes
  - AL, AR, CA, CT, DE, GA, HI, IL, IN, IA, KS, LA, ME, MD, MA, MI, MS, MT, NE, NH, NJ, OH, OK, OR, VT, VA, WV, WI
  - These would be joined by more states in the event of TCJA expiration

4. Impacts from Itemized Deduction Changes

- TCJA capped the State & Local Tax (SALT) deduction at $10,000 per filer and patched the Alternative Minimum Tax (AMT)
  - Both policies would reverse absent action
  - Most people who think they benefitted from SALT had it taken away by AMT
  - 36 states have adopted a SALT cap workaround, imposing state tax at the pass-through level
- TCJA reduced Mortgage Interest Deduction's maximum mortgage amounts from $1 million to $750,000, this would revert back
  - $750,000 in 2017 is about $1 million today, inflation-wise

4. Impacts from Itemized Deduction Changes



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5. Impacts from International & NOL Provisions

- TCJA adopted a new system of taxing income earned internationally, including GILTI, FDII, BEAT, and a one-time repatriation tax
  - Most states did not couple to GILTI or adopted a 95% exclusion, similar to a foreign dividend
  - 15 states tax GILTI, at levels ranging from 15% to 50%: CO, DC, DE, ID, ME, MD, MN, MT, NE, NH, OR, RI, UT, VT, WV
  - GILTI's federal rate increases starting 2026
- TCJA adopted 163(j) interest expense limitation, some states affirmatively decoupled from this calculation
- TCJA adopted limitations on net operating loss (NOL) provisions
  - TCJA: Unlimited carryforward capped at 80% of liability, no carrybacks
  - 19 states conform, 13 are more generous, the rest less generous

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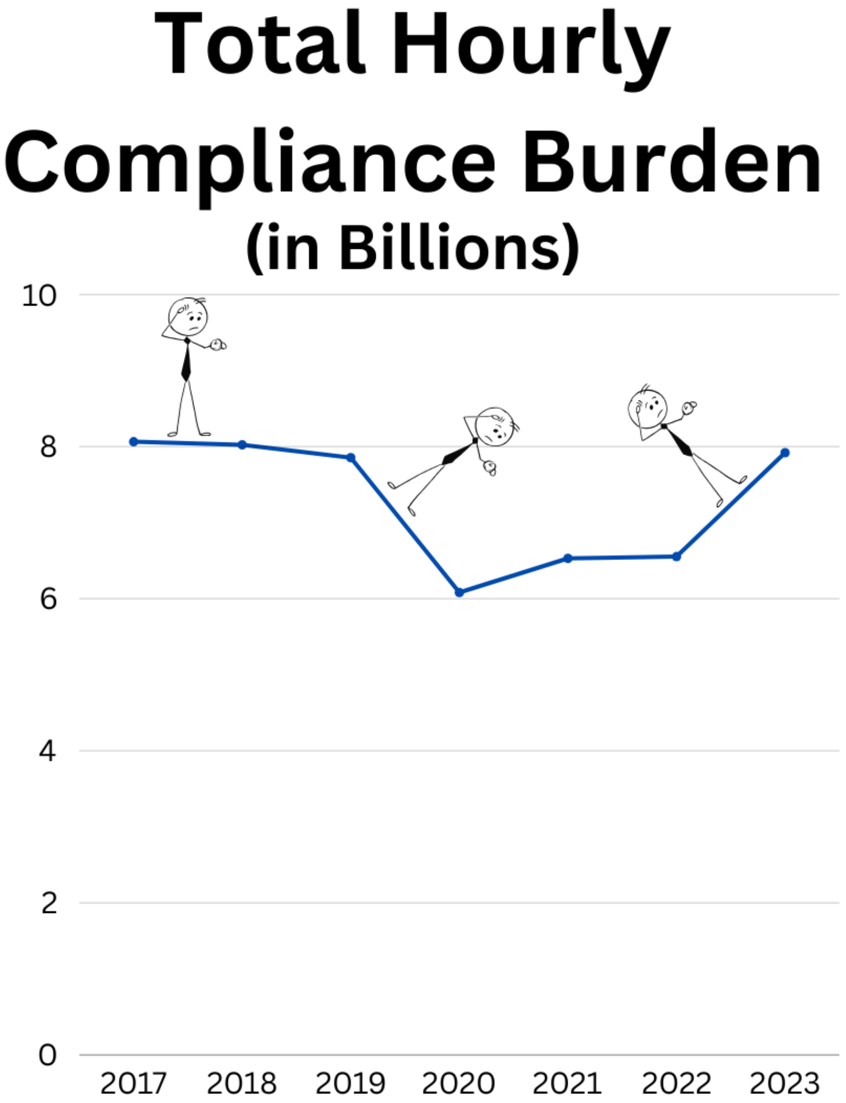
6. Impacts from Estate Tax Changes

- TCJA doubled the estate tax threshold: $13,610,000 in 2024
- Only 12 states & DC still have an estate tax
- Only Connecticut still couples to the federal estate tax threshold
  - DE, HI, and DC coupled pre-TCJA but have dropped it (DE repealed entirely)

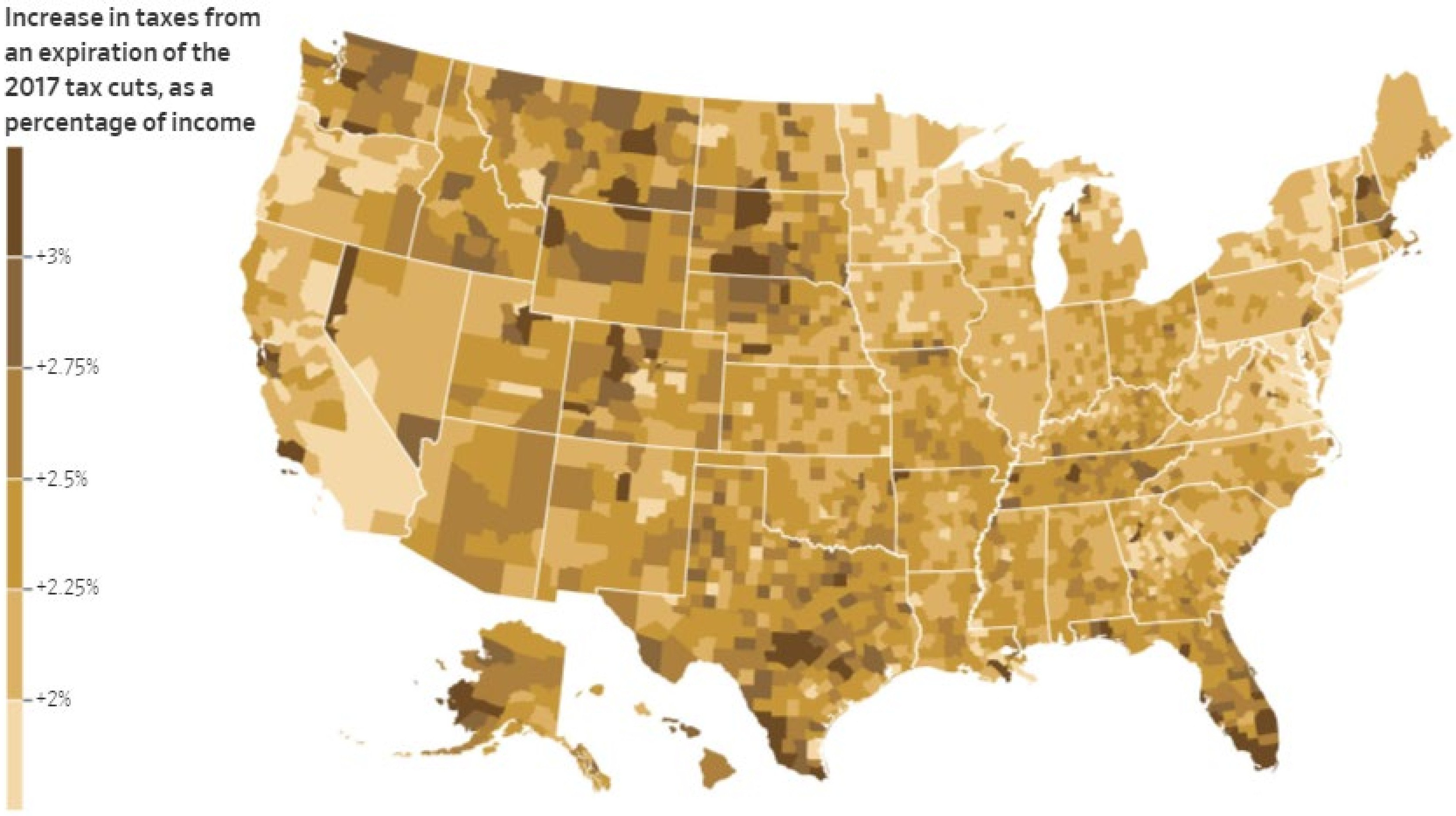
7. Impacts from Complexity Changes



8. Impacts from Expensing

- TCJA enacted 100 percent bonus depreciation, allowing businesses to deduct the full cost of capital expenditures in the year the cost is incurred
  - Phases out: 80% in 2023, 60% in 2024, 40% in 2025, 20% in 2026, 0% in 2027
- Mainly a timing shift, but a meaningful one for businesses engaged in capital investment
- Most states conform to federal expensing, even as it phases out.
  - Mississippi and Oklahoma adopted full expensing permanently for state taxes.
  - Connecticut decoupled from full expensing even when it was 100%.
- Strong impacts on economic growth, and its phaseout will impact state revenue to the extent it affects the economy.

9. Total Impact



10. Predictions

Policy	2017 (pre-TCJA)	2024 (TCJA)	2026 (if TCJA expires)
INDIVIDUAL TAXES			
Tax Rates	Seven brackets: 10%, 15%, 25%, 28%, 33%, 35%, 39.6%. Median-income Americans in the 25% bracket.	Seven brackets: 10%, 12%, 22%, 24%, 32%, 35%, 37%. Median-income Americans in the 22% bracket.	Seven brackets: 10%, 15%, 25%, 28%, 33%, 35%, 39.6%. Median-income Americans in the 25% bracket.
Standard Deduction	$6,350 (single), $12,700 (married), $9,350 (head of household). Approx. 70% of taxpayers take the standard deduction.	$14,600 (single), $29,200 (married), $21,900 (head of household). Approx. 90% of taxpayers take the standard deduction.	Reverts to 2017 level, adjusted for inflation
Personal Exemptions	$4,050 per exemption	$0	Reverts to 2017 level, adjusted for inflation
Limit on the Mortgage Interest Deduction	$1 million of indebtedness	$750,000 of indebtedness	$1 million of indebtedness
State and Local Tax (SALT) Cap	No cap, but limited by AMT	$10,000 per filer	No cap, but limited by AMT
Alternative Minimum Tax (AMT) Threshold	Applies above $54,300 (single) or $84,500 (married); exemption phases out entirely at $120,700 (single) or $160,900 (married)	Applies above $85,700 (single) or $133,300 (married); exemption phases out entirely at $609,350 (single) or $1,218,700 (married)	Reverts to 2017 levels, adjusted for inflation
Pease Limitation on Itemized Deductions	Deductions phase out above $261,500 (single) or $313,800 (married)	No phase out of deductions	Reverts to 2017 levels, adjusted for inflation
Child Tax Credit (CTC)	$1,000 per child, fully refundable, phased out above $75,000 (single) or $110,000 (married)	$2,000 per child, partially refundable, phased out above $200,000 (single) or $400,000 (married)	$1,000 per child, fully refundable, phased out above $75,000 (single) or $110,000 (married)
Estate Tax exemption level	$5,490,000	$13,610,000	Halves to 2017 levels, adjusted for inflation
BUSINESS TAXES			
Corporate Tax Rate	35%	21%	21%
Full Expensing of Capital Investments	TCJA set 100% bonus depreciation from 2017 through 2022, phasing down 20% each year beginning in 2023	60%	20%; in 2027 and after, normal depreciation rules apply
Territorial & Anti-Abuse Provisions	Worldwide tax system	Territorial, with GILTI (10.5%-13.125%), FDII (13.125%), and BEAT (10%)	Territorial, with GILTI (13.125%-16.406%), FDII (16.406%), and BEAT (12.5%)
Limit on Business Interest Deductibility	No limit	30% of earnings before interest and taxes (EBIT)	30% of earnings before interest and taxes (EBIT)
Pass-Through Business Tax Deduction	No deduction	Deduction equal to 20% of qualifying income, limited above $191,950 (single) or $383,900 (married)	No deduction
Net Operating Loss Rules	Fully deductible, can be carried forward 20 years or carried back 3 years	Deductible up to 80% of income, carryforward unlimited number of years, no carry-backs	Deductible up to 80% of income, carryforward unlimited number of years, no carry-backs

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