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IRC Update - Federal Legislation Enacted in 2021 and 2022 (General Fund Taxes -- Income and Franchise Taxes)

[LFB 2023-25 Budget Summary: Pages 193, #4]

BACKGROUND

State individual income tax and corporate income/franchise tax provisions regarding the amount of income subject to taxation are generally referenced to definitions under federal law. With limited exceptions, changes to federal law take effect for state tax purposes only after action by the Legislature. Each year, the Department of Revenue (DOR) typically reviews the federal law changes occurring in the previous year to assist in updating state references to the Internal Revenue Code (IRC). Under current law, state tax references generally refer to the code in effect on December 31, 2020.

The following federal laws that modified the IRC were enacted during 2021 and 2022: (a) American Rescue Plan Act of 2021 (ARPA); (b) Paycheck Protection Program Extension Act of 2021; (c) Surface Transportation Extension Act of 2021; (d) Further Surface Transportation Extension Act of 2021; (e) Infrastructure Investment and Jobs Act (IIJA); (f) Consolidated Appropriations Act of 2022 (CAA22); (g) Supreme Court Security Funding Act of 2022; (h) Inflation Reduction Act of 2022 (IRA); and (i) Consolidated Appropriations Act of 2023 (CAA23).

This paper discusses provisions of federal law that were recommended for state adoption under AB 43/SB 70, except for certain provisions under the TCJA that were removed from further consideration under Motion #10. Other federal law changes updating provisions that Wisconsin has not previously adopted are not discussed in this paper. Further, technical changes to federal law whose acceptance would not impact a person's state tax liability are not detailed below.

Upon further research and discussion with DOR, the fiscal estimates for certain provisions have been revised since introduction of AB 43/SB 70. This paper discusses provisions of CAA23 that were not reviewed by DOR in time to be included in AB 43/SB 70, but that could also be considered for state adoption by the Committee.

DISCUSSION POINTS

1. State references to federal law provide greater simplicity for taxpayers in preparing returns and reduce the administrative burden and cost for both taxpayers and DOR in assuring compliance with tax laws. The IRC references are used to determine which items of income are subject to taxation prior to specific state modifications.

2. The state uses separate tax rates and brackets and separate provisions regarding standard deductions, personal exemptions, itemized deductions, net operating loss, tax credits, excise taxes, and subtractions after the computation of federal adjusted gross income (AGI). Therefore, changes to these federal provisions typically have no effect for state tax purposes.

3. As introduced, AB 43/SB 70 would update references to the IRC under the individual income and corporate income/franchise tax to include certain federal tax provisions under eight federal laws retroactively and for taxable years beginning after December 31, 2022 [Alternative 1a]. This includes technical provisions and law changes which do not affect taxpayer liability as well as the provisions discussed below that would impact tax liability under state law. However, Alternatives 1a, 1b, and 1c would not include federal law changes made under CAA23.

4. In addition to updating references to the IRC, AB 43/SB 70 would also consolidate these provisions, generally defining the term "internal revenue code" in one location in the state statutes. Further, AB 43/SB 70 would recreate a conformity section so as to simplify the list of specific provisions subject to static conformity to the IRC in effect as of a certain date (such as depreciation conforming to the IRC in effect on January 1, 2014), and those provisions continuously conforming to all subsequent changes to the IRC (such as Section 179 expensing). The provision of AB 43/SB 70 that would provide for automatic adoption of all federal law changes impacting 529 college savings plans is discussed in LFB Paper #361. According to the Legislative Reference Bureau, consolidating the IRC into one location would reduce the number of pages in the printed statutes by seven pages.

5. Along with the federal law changes proposed under AB 43/SB 70, the Committee could also choose to update references to the IRC to include modifications to federal tax law under CAA23 [Alternatives 2a, 2b, and 2c].

6. The Attachment shows the estimated revenue impact from adopting the provisions that impact a taxpayer's tax liability from 2023-24 through 2032-33. As shown in the Attachment, state adoption of all provisions discussed in this paper [Alternative 2a] would result in a net increase to the general fund balance of an estimated $3.75 million in 2023-24 and $1.95 million in 2024-25 and would increase estimated expenditures under the federal temporary assistance for needy families (TANF) block grant by $0.95 million PR in 2023-24 and $1.15 million PR in 2024-25. The Attachment does not include federal provisions that have already been adopted automatically under current law, which have been included into state revenue estimates published by this office on May 15, 2023.

7. State adoption of temporary tax law changes provides simplicity for taxpayers and for DOR tax administration. However, because the adoption of temporary provisions that are subsequently extended can present challenges for state governments, the Committee could choose to

adopt only the permanent changes [Alternatives 1c and 2c]. Historically, Congress has enacted extensions and/or expansions of temporary tax reduction provisions that would require the Legislature to choose whether to continue maintaining conformity with the IRC provision or to allow that provision to sunset under current law. Extensions of temporary tax provisions can occur after DOR has printed guidance and made its forms available to practitioners for that tax year. In general, adoption of a federal tax provision that applies retroactively to previous tax years requires a taxpayer to file an amended return to receive the benefit, which can create administrative complexities for taxpayers and DOR.

8. The federal law changes under consideration that, if adopted, would impact a person's state tax liability are discussed in more detail below. Alternatives are also presented that would exclude federal tax law changes that are only temporary.

Permanent Tax Provisions

9. *Earned Income Tax Credit (EITC) - Disqualified Income Limit.* The federal EITC is a refundable credit based on income and family size and is calculated based on a percentage of earned income up to certain thresholds. The state EITC is calculated as a percentage of the federal credit that varies based on the claimant's number of qualifying children. The state credit is not available to claimants without qualifying children.

Under federal law, the EITC is denied to individuals having disqualified income in excess of a certain limit. Disqualified income is defined as taxable and nontaxable interest income, dividends, net income from nonbusiness rents and royalties, capital gain net income, and net passive income (if greater than zero) that is not self-employment income. The disqualified income limit was increased under ARPA for federal tax purposes beginning in tax year 2021. The limit is adjusted annually for inflation and is $11,000 for tax year 2023. However, state law has not adopted this ARPA provision, so the disqualified income limit for state tax purposes is $4,050 in tax year 2023. The state EITC is funded through a sum certain PR appropriation from the federal TANF block grant and a sum sufficient GPR appropriation. Therefore, adopting this provision beginning in tax year 2023 is estimated to increase TANF expenditures by $0.9 million in 2023-24 and $1.0 million in 2024-25 and GPR expenditures by $0.4 million in 2023-24 and 2024-25.

10. *EITC - Married Filing Separate.* Under federal law, married taxpayers must file using the married-joint filing status in order to claim the EITC. However, a provision in ARPA allows an exception to this filing requirement, beginning in tax year 2021, for an individual who: (a) files married-separate; (b) lives with their qualifying child (for purposes of the EITC) for more than half the year; and (c) during the last six months of the relevant tax year, did not live in the same principal dwelling as their spouse (or possesses a divorce or separation instrument relating to their spouse and is not a member of the same household as their spouse at the end of the relevant tax year). State adoption of this provision beginning in tax year 2023 is estimated to increase TANF expenditures by $50,000 in 2023-24 and $150,000 in 2024-25 and state GPR expenditures by $50,000 in 2023-24 and 2024-25. It should be noted that, for this provision and the preceding EITC provision, the Committee could instead choose to fully fund the estimated cost with GPR, rather than utilizing TANF funding for a portion of the cost.

11. *Repeal Worldwide Interest Deduction.* For taxable years beginning after December 31, 2020, multinational taxpayers were permitted to allocate interest expenses of a domestic group member on a worldwide basis. This altered the computation of the limitation on the foreign tax credit such that the interest expenses of foreign members of a worldwide affiliated group would have been considered in determining whether interest expenses of domestic members of the group must be allocated to foreign-sourced income. Initially enacted in 2004, federal law had delayed the effective date numerous times. ARPA permanently repealed the election such that it never took effect for federal tax purposes. Wisconsin neither has a state analogue to the foreign tax credit nor follows federal rules regarding taxation of foreign income. Thus, adopting the repeal of this provision retroactively for state purposes is estimated to have a minimal revenue impact because most of the income would be otherwise excluded under water's edge rules under state law.

12. *Multiple Declarations of Federally Declared Disasters.* Under current federal law, taxpayers affected by a federally-declared disaster, or terroristic or military action, are eligible to receive an extension of certain deadlines, such as the deadline to file a federal income tax return or to pay the associated tax. Prior to the IIJA, this extension period expired 60 days after the latest incident date specified in the initial disaster declaration. The IIJA specifies that, if multiple disaster declarations are issued within a 60-day time period, each declaration is considered a separate period. As a result, the extension period expires 60 days after the latest declaration was issued. The IIJA modifies the definition of a "disaster area" to mean an area in which a major disaster occurs for which the President of the United States provides financial assistance under certain other disaster assistance provisions of federal law. These changes took effect for federal disasters declared after the date of enactment and are estimated to decrease state tax revenues, if adopted retroactively for state tax purposes, by a minimal amount beginning in 2023-24.

13. *Significant Fires.* The IIJA expands the current law provision regarding certain deadline extensions for taxpayers affected by disasters or terroristic or military action (described above) to also include "a significant fire" as a qualifying event for extending such deadlines. The IIJA defines a significant fire as any fire with respect to which fire management assistance is provided under certain other provisions of federal law. This provision first applies to fires for which assistance is provided after November 15, 2021, and is estimated to decrease annual state tax revenues by a minimal amount, if adopted retroactively for state tax purposes, beginning in 2023-24.

14. *Exempt Facility Bonds - Carbon Dioxide Capture Facilities and Broadband Projects.* Interest earned on obligations that is tax-exempt under federal law generally must be added back to taxable income under state law. The IIJA provided that interest earned on obligations issued for qualified broadband projects after November 15, 2021, and for qualified carbon dioxide capture facilities after December 31, 2021, is exempt from federal income tax. Adoption of these provisions for state purposes beginning in tax year 2023 would decrease estimated individual income tax collections by $0.3 million in 2023-24 and 2024-25 and by $0.4 million annually beginning in 2025-26.

15. *Contributions to the Capital of Water and Sewerage Utilities.* Federal law provides that, for purposes of income tax, gross income does not include contributions to the capital of the taxpayer. However, contributions to capital does not include any: (a) contribution in aid of construction or any

other contribution as a customer or potential customer; or (b) contribution by any governmental entity or civic group (other than a contribution made by a shareholder as such). Provisions of the IIJA provide a special rule for water and sewerage disposal utilities, effective for taxable years beginning after December 31, 2020, such that any amount of money or other property received from any person (whether or not a shareholder) by a regulated public utility which provides water or sewerage disposal services generally qualifies as a contribution to capital, rather than gross income, if the following two requirements are met: (a) the amount is a contribution in aid of construction (not including amounts paid as service charges for starting or stopping services) or a contribution to the capital of the utility by a governmental entity providing for the protection, preservation, or enhancement of drinking water or sewerage disposal services; and (b) the amount (or any property acquired or constructed with such amount) is not included in the taxpayer's rate base for rate making purposes. In the case of a contribution in aid of construction which is property other than water or sewerage disposal facilities, certain expenditure rules apply to the amount contributed. Adopting the exclusion from gross income for state tax purposes beginning in tax year 2023 is estimated to reduce income and franchise tax revenues by $1.2 million in 2023-24 and $1.0 million in 2024-25, with the fiscal effect gradually declining to a revenue reduction of $0.3 million in 2031-32.

16. *Energy Efficient Commercial Buildings.* Effective beginning in tax year 2023, provisions of the IRA increased the availability and size of the energy-efficient commercial buildings deduction in Section 179D of the IRC from $1.80 per square foot to up to $5.00 per square foot for certain eligible properties. Further, the IRA also set a special rule allowing real estate investment trusts to reduce earnings and profits in the year the energy-efficient components are placed into service (for retrofit property, the year of final certification). Previously, real estate investment trusts had to reduce earnings and profits ratably over a five-year period. The provisions relating to the deduction for energy efficient commercial buildings are adopted automatically pursuant to current law. However, the state is not federalized to federal definitions for earnings and profits (which determine whether a distribution by a corporation is a dividend and/or taxable income). Adopting the provision allowing real estate investment trusts to reduce earnings in the year the components are placed into service, instead of ratably, is estimated to have a minimal effect on state revenues.

17. *Elective Payment of Applicable Credits.* Provisions of the IRA allow certain organizations (such as tax-exempt entities and state, local, and tribal governments), for taxable years beginning after December 31, 2022, to elect to treat certain federal tax credits for energy property/renewable energy as if they were payments of tax. As a result, payments in excess of tax liability can be refunded to these organizations. Taxpayers who are not tax-exempt entities are allowed a one-time transfer of these tax credits to an unrelated taxpayer. Any payments received in exchange for the transfer of credits are excluded from income, and any amounts paid in order to obtain a transferred credit cannot be deducted from income. Wisconsin has not adopted these federal credits, and thus the provisions relating to refunds do not apply for state tax purposes. Further, any payments received in exchange for transferring the credits are not excludable and amounts paid to receive a credit are not deductible under current state law. However, adopting the IRA provisions relating to the treatment of payments made/received for transfer of the credits would enable these tax-exempt organizations to transfer the credits without incurring state tax liability. It is estimated that adopting these provisions would have a minimal effect on state revenues.

18. *Deferral of Tax for Certain Sales of Employer Stock to Employee Stock Ownership Plan (ESOP) Sponsored by a Tax-Option (S) Corporation.* An ESOP enables employees to own a portion or all of their employer. Effective for taxable years beginning after December 31, 2027, CAA23 would allow the owner of employer stock issued by an S corporation to defer 10% of the long term capital gain from the sale of that stock to an ESOP (if it owns at least 30% of the corporation's stock). This provision would reduce state tax revenues beginning in 2027-28 by $0.7 million, with the reduction growing to $5.1 million in 2032-33.

19. *Achieving a Better Life Experience (ABLE) Age Requirement.* Under federal law, a qualified ABLE program may be established by any state for the purpose of meeting the qualified disability expenses of a designated beneficiary, generally an individual whose blindness or disability occurred before age 26. In general, federal law permits up to $17,000 of contributions (total from all contributors) in tax year 2023 to be deposited into an ABLE account per designated beneficiary per calendar year. The maximum annual contribution limit is indexed to adjustments made to the annual exclusion amount under the federal gift tax. Wisconsin has adopted the federal tax treatment of ABLE accounts and allows a state deduction for any eligible contribution deposited by an account owner, or any other person, for the year in which a contribution is made into any state's federally qualified ABLE account.

CAA23 increases the age limit for the initial occurrence of the blindness or disability of a qualified ABLE account beneficiary from 26 to 46, beginning in tax year 2026. Concurrent state adoption of this provision is estimated to reduce individual income tax collections by $0.3 million in 2026-27, growing to a revenue reduction of $2.5 million in 2031-32.

20. *College Savings Plan Rollovers to Roth Accounts.* For distributions taken on or after January 1, 2024, a provision of CAA23 enables 529 account beneficiaries to roll amounts remaining in a 529 account over to a Roth individual retirement account (IRA) without penalty upon distribution, up to a lifetime maximum of $35,000. To receive this preferential treatment, the 529 account must have been open for at least 15 years, and the Roth IRA must be maintained for the benefit of the beneficiary. No amounts which were contributed within five years of the distribution date may be rolled over. Annual IRA contribution limits also apply to any amounts rolled over from a 529 account. For tax year 2023, the aggregate limit for contributions to any IRA is $6,500, with an additional $1,000 allowed for taxpayers aged 50 and over. Concurrent state adoption of this provision would reduce estimated individual income tax collections by $0.8 million in 2023-24 and $2.0 million in 2024-25, growing to a revenue reduction of $3.0 million annually beginning in 2027-28. However, if adopted under LFB Paper #361, this provision would not have an additional fiscal impact.

21. *Credit for Small Employer Pension Plan Startup Costs.* Federal law provides a three-year credit for small employers (having fewer than 100 employees) for up to 50% of certain administrative costs up to an annual maximum of $5,000. Effective for taxable years beginning after December 31, 2019, CAA23 clarifies that the credit applies to employers that join an existing plan. Effective for taxable years beginning after December 31, 2022, CAA23 would increase the federal credit for small business pension plan startup costs to up to 100% of administrative costs for employers having 50 or fewer employees. Further, CAA23 provides additional credit of up to $1,000 per employee equal to the applicable percentage of eligible employer contributions, which phases out for employers having between 51 to 100 employees.

Under federal law, a taxpayer may elect to take the credit, but may not both claim the credit and a deduction for the same expenses. Thus, under current state law, a taxpayer would need to make an adjustment to federal gross income on the Wisconsin income/franchise tax return to allow a deduction for these expenses. According to DOR, if the federal provisions were adopted, the taxpayer would have the option of making a different election for state tax purposes (such that they would claim the credits for federal purposes and take deductions for state purposes). These provisions would have a minimal effect on state tax revenues.

22. *Limitation on Deduction for Qualified Conservation Contributions.* Under federal law, "qualified conservation contributions" are charitable donations of real property interests designated for purposes of conservation. Provisions of CAA23 specify that, in general, contributions made after December 29, 2022, by a pass-through entity will not be treated as a qualified conservation contribution if the amount exceeds 2.5 times the sum of each owner's relevant basis in the pass-through entity. Certain exceptions are provided for family partnerships, contributions to preserve certified historic structures, and when a three-year holding period has been met. If the deduction is disallowed and tax is due, the taxpayer is subject to underpayment interest. Also, if the deductions are disallowed, they are treated as a tax avoidance transaction. Adoption of this provision (retroactively to contributions made on December 30, 2022) would increase state revenues by $8.2 million in 2023-24 and $6.4 million in 2024-25, with the effect decreasing to an increase of $3.3 million annually starting in 2027-28.

23. Table 1 displays the net fiscal effect of state adoption of all the permanent provisions described above. These provisions are estimated to increase the general fund balance by $5.45 million in 2023-24, $2.65 million in 2024-25, and $1.35 million in 2025-26, and decrease the balance by $0.95 million in 2026-27, growing to a decrease of $8.45 million annually beginning in 2032-33. In addition, PR (TANF) expenditures (which do not affect the general fund) would increase by $0.95 million in 2023-24 and $1.15 million annually beginning in 2024-25.

TABLE 1

IRC Update - State Adoption of Permanent Provisions, Net Fiscal Effect to the General Fund (Millions)

	2023-24	2024-25	Fund Source
Recommended under AB 43/SB 70			
EITC - Disqualified Income Limit	$0.40	$0.40	GPR
	0.90	1.00	PR (TANF)
EITC - Married Filing Separate	0.05	0.05	GPR
	0.05	0.15	PR (TANF)
Repeal Worldwide Interest Deduction	Minimal	Minimal	GPR-Tax
Multiple Declarations of Federally Declared Disasters	Minimal	Minimal	GPR-Tax
Significant Fires	Minimal	Minimal	GPR-Tax
Exempt Facility Bonds	-0.30	-0.30	GPR-Tax
Energy Efficient Commercial Buildings	Minimal	Minimal	GPR-Tax
Contributions to the Capital of Water and Sewerage Utilities	-1.20	-1.00	GPR-Tax
Elective Payment of Applicable Credits	Minimal	Minimal	GPR-Tax
Subtotal	$0.45	$0.45	GPR
Subtotal	0.95	1.15	PR (TANF)
Subtotal	-1.50	-1.30	GPR-Tax
CAA23			
Deferral of Tax for Certain Sales of ESOP Sponsored by S Corporation	N/A	N/A	GPR-Tax
ABLE Age Requirement	N/A	N/A	GPR-Tax
College Savings Plan Rollovers to Roth Accounts	-$0.80	-$2.00	GPR-Tax
Credit for Small Employer Pension Plan Startup Costs	Minimal	Minimal	GPR-Tax
Limitation on Deduction for Qualified Conservation Contributions	8.20	6.40	GPR-Tax
Subtotal	$7.40	$4.40	GPR-Tax
Total	$0.45	$0.45	GPR
Total	0.95	1.15	PR (TANF)
Total	5.90	3.10	GPR-Tax
Net Effect to General Fund	$5.45	$2.65	

Temporary Tax Provisions

24. *Student Loan Forgiveness.* With certain exceptions, forgiven student loans are generally considered taxable income under federal law. ARPA stipulates that any forgiven student loan that was expressly provided for postsecondary educational expenses and meets certain other requirements is excluded from taxable income for tax years 2021 through 2025. If the state were to adopt this provision, it is estimated that individual income tax revenues would decrease by a minimal amount annually through 2025-26.

The Administration indicates that the fiscal effect of this provision is assumed to be minimal following recent court decisions (*Biden v. Nebraska* and *Department of Education v. Brown*) which vacated the federal student loan discharge program that would have discharged up to $10,000 (or up to $20,000 for Pell Grant recipients) of student loan debt for borrowers that satisfy certain income limits. However, if the student loan discharge program were upheld on appeal, state adoption of this provision of ARPA could result in foregone revenues of several hundred million dollars in the 2023-25 biennium (depending on the outcome of future court cases). Because of the magnitude and uncertainty of the fiscal effect associated with adopting the provision, Alternatives 1b and 2b are presented to exclude this provision.

25. *High Deductible Health Plans (HDHPs) - Remote Care*. Federal law allows taxpayers to create a health savings account (HSA) if they meet certain requirements, such as that the individual: (a) is covered under an HDHP; and (b) cannot be claimed as a dependent on another individual's tax return. Contributions to an HSA by the employee and their employer, and the associated interest earnings, are deductible from gross income, as are account distributions if used to pay for qualified medical expenses. CAA22 provides that, for plan months beginning after March 31, 2022, and before January 1, 2023, a health plan may still be considered an HDHP even if it fails to require a deductible for telehealth and other remote care services. This extends a provision initially enacted under CARES that was adopted for state tax purposes under 2019 Act 185. Retroactive state adoption of this provision of CAA22 would decrease estimated individual income tax collections by $0.4 million on a one-time basis in 2023-24.

26. *HDHP Extension*. For plan years beginning after December 31, 2022, and before January 1, 2025, CAA23 extends the preceding provision of CAA22 that maintains the treatment of HDHPs which fail to require a deductible for telehealth and other remote care services. State adoption of this provision would reduce estimated individual income tax collections by $1.3 million in 2023-24 and $0.7 million in 2024-25.

27. *Aviation Fuel Credit - Definition of Gross Income*. Provisions of the IRA create a sustainable aviation fuel credit ($1.25 per gallon) for certain fuel mixtures sold or used after December 31, 2022, and before January 1, 2025. The credit does not apply for state purposes, but the credit amount affects the computation of federal gross income. Conforming state law to the definition of federal gross income by adopting the provision would have a minimal revenue effect.

28. Table 2 depicts the fiscal effects of state adoption of these temporary federal tax provisions. These provisions are estimated to reduce the general fund balance by $1.7 million in 2023-24 and $0.7 million in 2024-25, and are estimated to have a minimal impact on general fund revenues thereafter.

TABLE 2

**IRC Update - State Adoption of Temporary Provisions,
Net Fiscal Effect to the General Fund (Millions)**

	2023-24	2024-25	2025-26 (and thereafter)	Fund Source
Recommended Under AB 43/SB 70				
Student Loan Forgiveness	Minimal	Minimal	Minimal	GPR-Tax
High Deductible Health Plans - Remote Care	-$0.4	Minimal	Minimal	GPR-Tax
Aviation Fuel Credit	Minimal	Minimal	Minimal	GPR-Tax
CAA23				
High Deductible Health Plans - Extension	-1.3	-$0.7	Minimal	GPR-Tax
Total	-$1.7	-$0.7	Minimal	GPR-Tax

29. The Committee may decide to adopt only those federal provisions that were included in AB 43/SB 70 [Alternative 1a], or may decide to also include the provisions of CAA23 [Alternative 2a]. As shown in the Attachment, adopting the provisions of AB 43/SB 70 (Alternative 1a) is estimated to: (a) reduce income and franchise tax revenues by $1.9 million in 2023-24 and $1.3 million in 2024-25; and (b) increase tax credit expenditures by $0.45 million GPR and $0.95 million PR in 2023-24 and $0.45 million GPR and $1.15 million PR in 2024-25. If the Committee chose to also adopt the provisions of CAA23 [Alternative 2a], the overall increase in income and franchise tax collections would be $4.2 million in 2023-24 and $2.4 million in 2024-25 [changes to GPR and PR expenditures would be the same as under Alternative 1a].

30. By contrast, the Committee could choose to adopt only those provisions which were included in AB 43/SB 70 and are permanent [Alternative 1c]. As shown in Table 1, this alternative is estimated to: (a) decrease income and franchise tax revenues by $1.5 million in 2023-24 and $1.3 million in 2024-25; and (b) increase tax credit expenditures by $0.45 million GPR and $0.95 million PR in 2023-24 and by $0.45 million GPR and $1.15 million PR in 2024-25. Alternatively, the Committee could decide to also include the permanent provisions of CAA23 [Alternative 2c]. Such a proposal is estimated to increase income and franchise tax collections by $5.9 million in 2023-24 and $3.1 million in 2024-25 [changes to GPR and PR expenditures would be the same as under Alternative 1c].

ALTERNATIVES

1. Adopt Provisions Recommended under AB 43/SB 70

a. *Permanent and Temporary Provisions.* Adopt the federal tax provisions identified above, including revisions to state statutes to simplify the legal references to the federal IRC. Estimate reduced income and franchise tax collections of $1,900,000 in 2023-24 and $1,300,000 in 2024-25. Estimate increased TANF expenditures for refundable tax credits of $950,000 in 2023-24 and $1,150,000 in 2024-25 and increased GPR expenditures of $450,000 in 2023-24 and 2024-25.

ALT 1a	Change to Base
GPR	$900,000
PR (TANF)	2,100,000
Total	$3,000,000
GPR-Tax	-$3,200,000

b. *Remove Student Loan Forgiveness Provision.* Adopt Alternative 1a, but remove the student loan provision described in Discussion Point #24.

ALT 1b	Change to Base
GPR	$900,000
PR (TANF)	2,100,000
Total	$3,000,000
GPR-Tax	-$3,200,000

c. *Adopt Only Permanent Provisions.* Adopt Alternative 1a, but do not adopt the temporary provisions identified above. Estimate reduced income and franchise tax collections of $1,500,000 in 2023-24 and $1,300,000 in 2024-25. Estimate increased TANF expenditures for refundable tax credits of $950,000 in 2023-24 and $1,150,000 in 2024-25 and increased GPR expenditures of $450,000 in 2023-24 and 2024-25.

ALT 1c	**Change to Base**
GPR	$900,000
PR (TANF)	2,100,000
Total	$3,000,000
GPR-Tax	-$2,800,000

2. Adopt AB 43/SB 70 Provisions and CAA23 Provisions

a. Permanent and Temporary Provisions. Adopt Alternative 1a and also adopt the federal tax provisions under CAA23. Estimate increased income and franchise tax collections of $4,200,000 in 2023-24 and $2,400,000 in 2024-25. Estimate increased TANF expenditures for refundable tax credits of $950,000 in 2023-24 and $1,150,000 in 2024-25, and increased GPR expenditures of $450,000 in 2023-24 and 2024-25.

ALT 2a	**Change to Base**
GPR	$900,000
PR (TANF)	2,100,000
Total	$3,000,000
GPR-Tax	$6,600,000

b. Remove Student Loan Forgiveness Provision. Adopt Alternative 2a, but remove the student loan provision described in Discussion Point #24.

ALT 2b	**Change to Base**
GPR	$900,000
PR (TANF)	2,100,000
Total	$3,000,000
GPR-Tax	$6,600,000

c. *Adopt Permanent Provisions Only*. Adopt Alternative 2a, with the modification to adopt only the permanent federal tax provisions. Estimate an increase in income and franchise tax collections of $5,900,000 in 2023-24 and $3,100,000 in 2024-25. Estimate increased TANF expenditures for refundable tax credits of $950,000 in 2023-24 and $1,150,000 in 2024-25, and increased GPR expenditures of $450,000 in 2023-24 and 2024-25.

ALT 4	**Change to Base**
GPR	$900,000
PR (TANF)	2,100,000
Total	$3,000,000
GPR-Tax	$9,000,000

3. Take no action.

Prepared by: John Gentry and Dan Spika
Attachment

ATTACHMENT

State Adoption of Federal Provisions Adopted in 2021 and 2022, Net Fiscal Effect (Millions)

	2023-24	2024-25	2025-26	2026-27	2027-28	2028-29	2029-30	2030-31	2031-32	2032-33	Fund Source
AB 43/SB 70 Recommended Provisions											
Permanent Provisions											
EITC - Disqualified Income Limit	$0.40	$0.40	$0.40	$0.40	$0.40	$0.40	$0.40	$0.40	$0.40	$0.40	GPR
	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	PR (TANF)
EITC - Married Filing Separate	0.05	0.05	0.05	0.05	0.05	0.05	0.05	0.05	0.05	0.05	GPR
	0.05	0.15	0.15	0.15	0.15	0.15	0.15	0.15	0.15	0.15	PR (TANF)
Repeal Worldwide Interest Deduction	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	GPR-Tax
Multiple Declarations of Federally Declared Disasters	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	GPR-Tax
Significant Fires	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	GPR-Tax
Exempt Facility Bonds	-0.30	-0.30	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	GPR-Tax
Contributions to the Capital of Water and Sewerage Utilities	-1.20	-1.00	-0.90	-0.80	-0.60	-0.50	-0.50	-0.40	-0.30	-0.30	GPR-Tax
Energy Efficient Commercial Buildings	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	GPR-Tax
Elective Payment of Applicable Credits	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	GPR-Tax
Temporary Provisions											
Student Loan Forgiveness*	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	GPR-Tax
High Deductible Health Plans - Remote Care	-$0.40	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	GPR-Tax
Aviation Fuel Credit	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	GPR-Tax
Subtotal	$0.45	$0.45	$0.45	$0.45	$0.45	$0.45	$0.45	$0.45	$0.45	$0.45	GPR
Subtotal	0.95	1.15	1.15	1.15	1.15	1.15	1.15	1.15	1.15	1.15	PR (TANF)
Subtotal	-1.90	-1.30	-1.30	-1.20	-1.00	-0.90	-0.90	-0.80	-0.70	-0.70	GPR-Tax
CAA23											
Permanent Provisions											
Deferral of Tax for Certain Sales of ESOP Sponsored by S Corp.	N/A	N/A	N/A	N/A	-$0.70	-$1.70	-$2.70	-$3.70	-$5.10	-$5.10	GPR-Tax
ABLE Age Requirement	N/A	N/A	N/A	-$0.30	-0.70	-1.00	-1.40	-1.90	-2.50	-2.50	GPR-Tax
College Savings Plan Rollovers to Roth Accounts	-$0.8	-$2.00	-$2.40	-2.80	-3.00	-3.00	-3.00	-3.00	-3.00	-3.00	GPR-Tax
Credit for small employer pension plan startup costs	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	GPR-Tax
Limitation on Deduction for Qualified Conservation Contributions	8.20	6.40	5.50	3.80	3.30	3.30	3.30	3.30	3.30	3.30	GPR-Tax
Temporary Provisions											
High Deductible Health Plan Extension	-$1.30	-$0.70	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	Minimal	GPR-Tax
Subtotal	$6.10	$3.70	$3.10	$0.70	-$1.10	-$2.40	-$3.80	-$5.30	-$7.30	-$7.30	GPR-Tax
Both AB 43/SB 70 and CAA23 Provisions											
Total	$0.45	$0.45	$0.45	$0.45	$0.45	$0.45	$0.45	$0.45	$0.45	$0.45	GPR
Total	0.95	1.15	1.15	1.15	1.15	1.15	1.15	1.15	1.15	1.15	PR (TANF)
Total	4.20	2.40	1.80	-0.50	-2.10	-3.30	-4.70	-6.10	-8.00	-8.00	GPR-Tax
Net Effect on General Fund	$3.75	$1.95	$1.35	-$0.95	-$2.55	-$3.75	-$5.15	-$6.55	-$8.45	-$8.45	

*Cost may be higher depending on court case