Assigned to FIN FOR COMMITTEE

ARIZONA STATE SENATE

Fifty-Fourth Legislature, First Regular Session

FACT SHEET FOR S.B. 1166

conformity; internal revenue code; exceptions

Purpose

An emergency measure that partially conforms Arizona tax statutes to the Internal Revenue Code (IRC) as of January 1, 2018.

Background

The Arizona Legislature periodically updates statutory definition of the IRC to include any federal provisions that became effective in the preceding calendar year as a means of paralleling the computation of Arizona income tax and other statutory references throughout the Arizona Revised Statutes to the amended IRC. Tax conformity with the IRC is deemed necessary because the calculation of Arizona corporate income tax liability begins with federal taxable income. Similarly, Federal Adjusted Gross Income is the starting point for individual income tax assessment.

The federal Tax Cuts and Jobs Act (U.S. TCJA) enacted on December 22, 2017, includes over 100 provisions and represents the largest revision to the IRC in more than 30 years. The latest estimate of impact detailed by the Joint Legislative Budget Committee (JLBC) states that the impact of fully conforming to these IRC changes would be a revenue gain of approximately $155,000,000.

JLBC indicates that the major provisions we would be conforming to cannot be modeled by the Arizona Department of Revenue. JLBC projects that the impact of conforming to these provisions would be a net $10,000,000 revenue gain in FY 2019.

Provisions

Conformity

1. Updates the statutory definition of the IRC to include provisions in effect as of January 1, 2018. Repeals this provision on January 1, 2020.

2. Decouples several provisions from the U.S. TCJA:
   a) caps state taxes and local taxes at $10,000;
   b) caps mortgage interest and limits home equity;
   c) eliminates two percent business and/or employee expenses;
   d) repeals overall cap on itemized deductions;
   e) limits pass-through losses to $250,000/$500,000; and
   f) allows higher bonus depreciation or business expensing.

3. Accomplishes decoupling from these provisions by creating the following additions and subtractions from Arizona taxable income:

Individual Additions to Taxable Income

4. Adds the following amounts to Arizona gross income:
   a) the depreciation allowable under section 167(a) of the IRC as if the additional allowance had been the full amount allowed pursuant to section 168(k) of the IRC; and
   b) any amount deducted under IRC section 179 relating to expensing certain business assets.

5. Adds the amount that would have been excluded pursuant to section 68 of the IRC relating to the overall limitation on itemized deductions.

6. Repeals this section on January 1, 2020.

Individual Itemized Deductions

7. Allows the taxpayer to deduct in lieu of the standard deduction:
   a) the amount of state taxes and local taxes paid to the extent that they were not deducted in computing federal taxable income;
   b) miscellaneous itemized deductions to the extent that the aggregate amount of miscellaneous itemized deductions exceeds two percent of federal adjusted gross income and was not deducted in computing federal taxable income;
   c) home equity indebtedness interest and acquisition indebtedness interest to the extent that it was not deducted in computing federal taxable income;
   d) business losses of a pass-through entity to the extent that they were not deducted in computing federal taxable income. If the deduction is taken, the taxpayer may not deduct the amount of business losses carried over from the taxable year beginning from and after December 31, 2017, through December 31, 2018;
   e) an amount equal to the depreciation allowable in the IRC for the taxable year as computed as if the additional allowance for depreciation had been 50 percent of the amount allowed; and
   f) the amount deducted related to expensing certain business assets not to exceed $500,000 or $500,000 minus the amount by which the cost of that property placed in service during the taxable year exceeds $2,000,000, whichever is less.

8. Repeals this section on January 1, 2020.

Corporate Additions to Taxable Income

9. Requires the corporate taxpayer, for tax year 2018, to add any amount deducted pursuant to IRC section 179 relating to expensing certain business assets to the extent not previously added.

10. Repeals this section on January 1, 2020.

Corporate Subtractions from Taxable Income

11. Requires the corporate taxpayer, for tax year 2018, to subtract from Arizona gross income the amount deducted related to expensing certain business assets not to exceed $500,000 or $500,000 minus the amount by which the cost of that property placed in service during the taxable year exceeds $2,000,000, whichever is less.

12. Repeals this section on January 1, 2020.

Miscellaneous

13. Makes technical and conforming changes.

14. Applies retroactively to tax year 2018.

15. Becomes effective on signature of the Governor, if the emergency clause is enacted.

Prepared by Senate Research
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CS/kja