Income Tax Conformity and the CARES Act

Open Sky Policy Institute
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The CARES Act

- Signed into law on March 27th in response to COVID-19 pandemic

- Contained a number of provisions assisting taxpayers and state and local governments
  - PPP, EIP, grants, tax changes

CARES Act: Impact on Nebraska

- Nebraska has received billions in federal funds to assist with the pandemic
  - PPP: $3.4 billion in funds to Nebraska businesses
  - EIP: $1.6 billion to Nebraska residents
  - Over $1 billion in grants to help cities, counties, and businesses in need, including approx. $400M for agriculture and other business relief ($230M for small business stabilization)

- Federal tax cuts for certain taxpayers

Federal Tax Cuts → Nebraska Tax Cuts

- Nebraska is a "rolling conformity" state
- Legislature delegates tax writing to Congress and has to affirmatively opt out
- DOR estimates that conformity to CARES Act provisions will cost Nebraska $250 million of tax revenue over the next three years

Nebraska and Conformity

- The big question: Should Nebraska give $250 million of income tax cuts in the midst of the pandemic?

Nebraska and Conformity

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  - All of those who get cuts will directly benefit and many of them will need assistance.

Nebraska and Conformity

- The big question: Should Nebraska give $250 million of income tax cuts?
  - What gets cut or whose taxes get raised?
  - Why would we do that?
    - If stimulus, is this the best way?

Major Tax Provisions in CARES Act

- Individual Income Tax:
  - ATL charitable deduction, increased deduction allowance
  - Temporary exclusion for certain student loan payments by employers
  - Special rules for retirement fund distributions / loans
  - Temporary waiver of RMD rules
  - Modified NOL rules
  - Expanded Excess Business Loss provision

Provisions	Estimated Revenue Change
Charitable Contribution Changes	($6M)- ATL Deduction ($3M) – Limitation
Student Loan Provisions	(600k)
Retirement Fund Rules	$3.5M
RMD Rules	($13M)
Modified NOLs (Individual)	*With corporate*
Excess Business Loss Expansion	($187M)

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Excess Business Losses

- TCJA added limitation on "excess business losses"
  - No more than $500,000 (inflation adjusted) of losses from pass though businesses can be used to offset other income in any year
  - Needless to say, need to be at a very high income level to be impacted by this

Excess Business Losses

- CARES Act suspends that rule retroactively to 2018
  - For example, a taxpayer who generated a profit this year, but who had large losses in 2018 or 2019 would get to apply this provision and obtain a refund of taxes paid in earlier years.

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- CARES Act suspends that rule retroactively to 2018
  - For example, a taxpayer who generated a profit this year, but who had large losses in 2018 or 2019 would get to apply this provision and obtain a refund of taxes paid in earlier years.
  - That applies regardless of their 2020 income / losses or, obviously, what other aid they got under the CARES Act

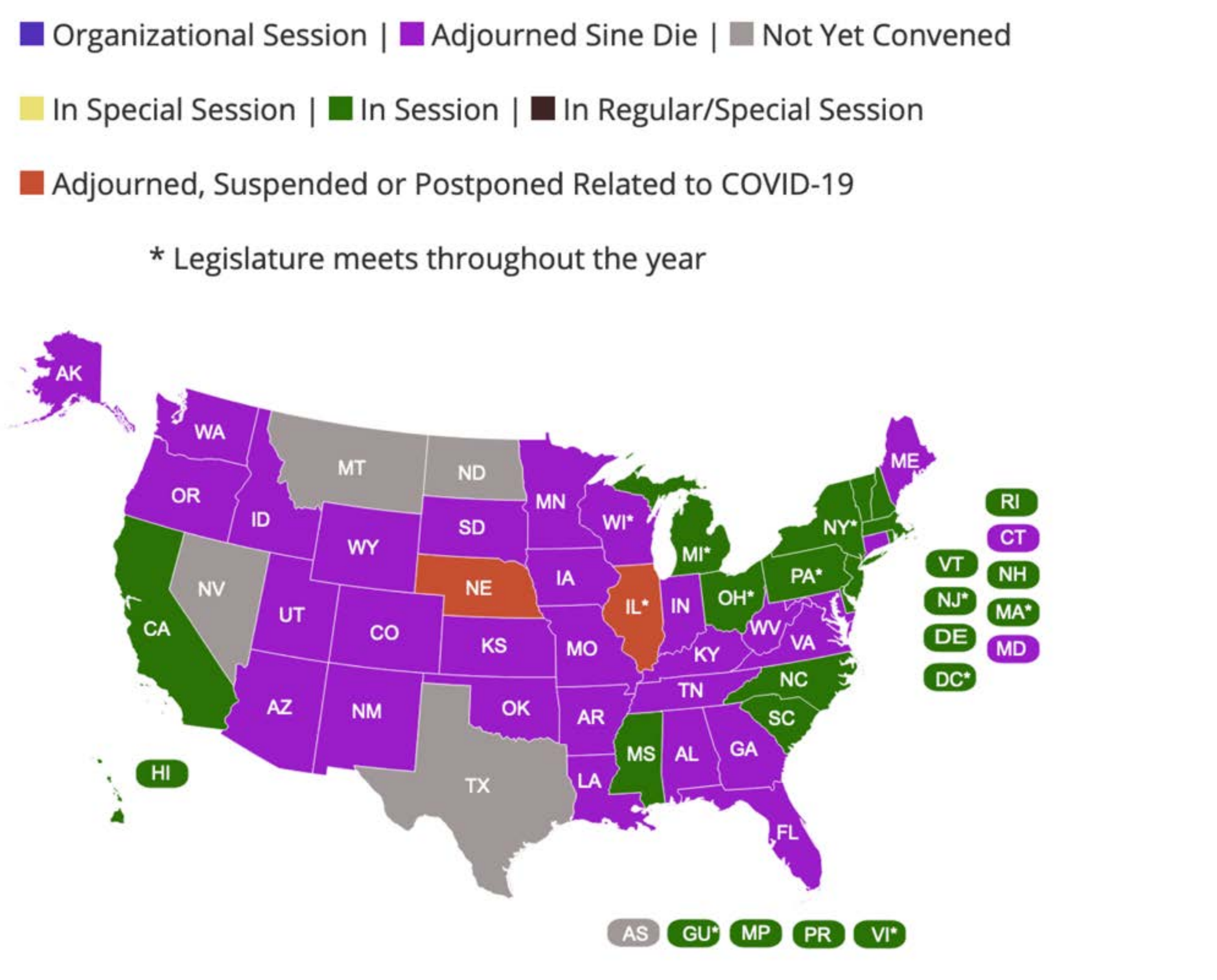
Major Tax Provisions in CARES Act

- Corporate Income Tax:
  - Refundable employee retention credit
  - PPP Loan Forgiveness
  - Modified NOL Rules
  - Increased charitable deductions
  - Increased business interest limit
  - Retroactively expanded full expensing

Provisions	Estimated Revenue Change
Employee retention credit	$5M
PPP Loan Forgiveness	??
Modified NOL Rules	($18M)
Charitable Deduction	($4M)
Interest Deduction	($17.5M)
Full Expensing	??

Other States

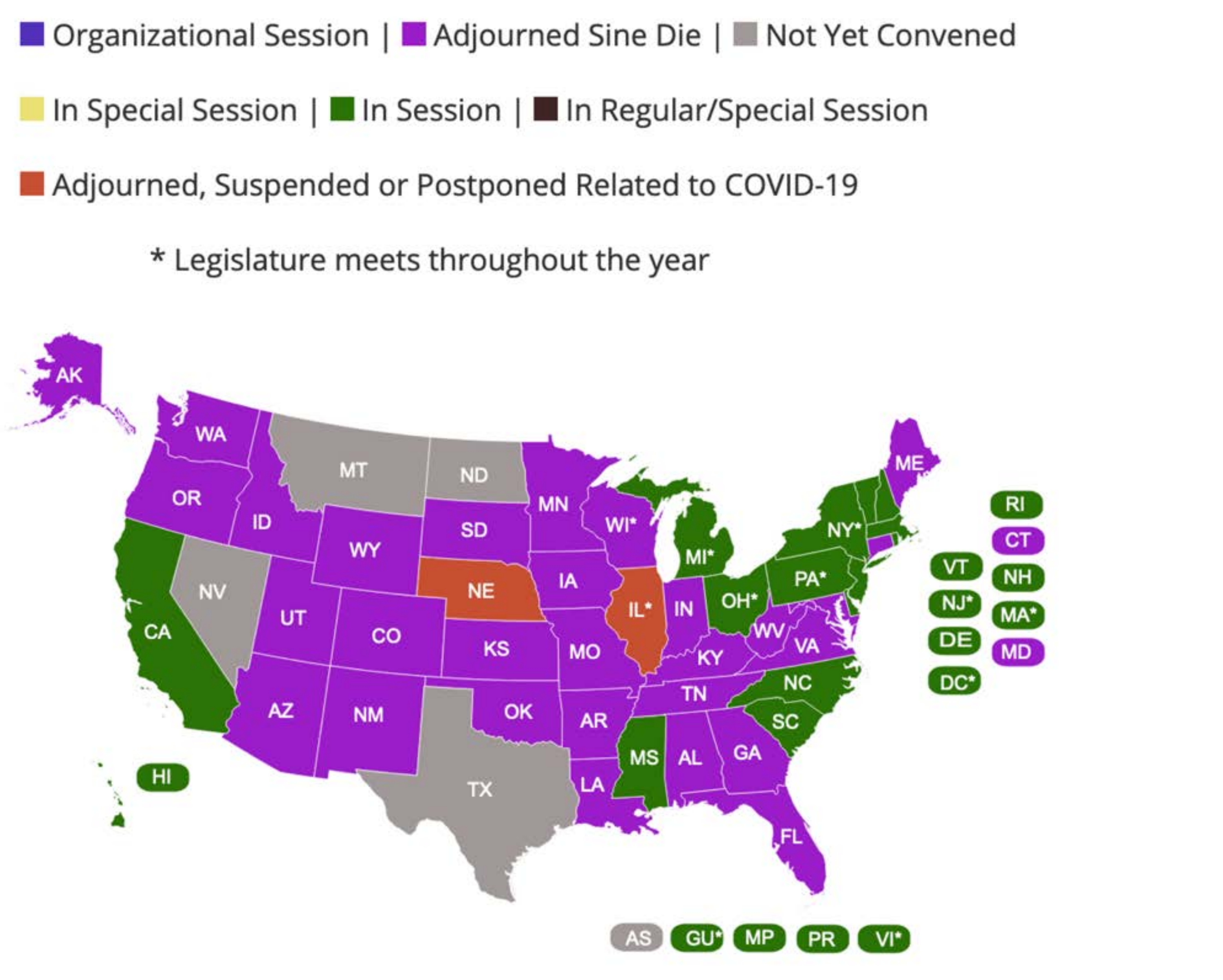
- Few states are in session right now



* Information from NCSL

Other States

- Few states are in session right now
- Of those, only DE, NY, and RI are rolling states
  - NY decoupled
  - RI losses estimated at $17.5M over two years



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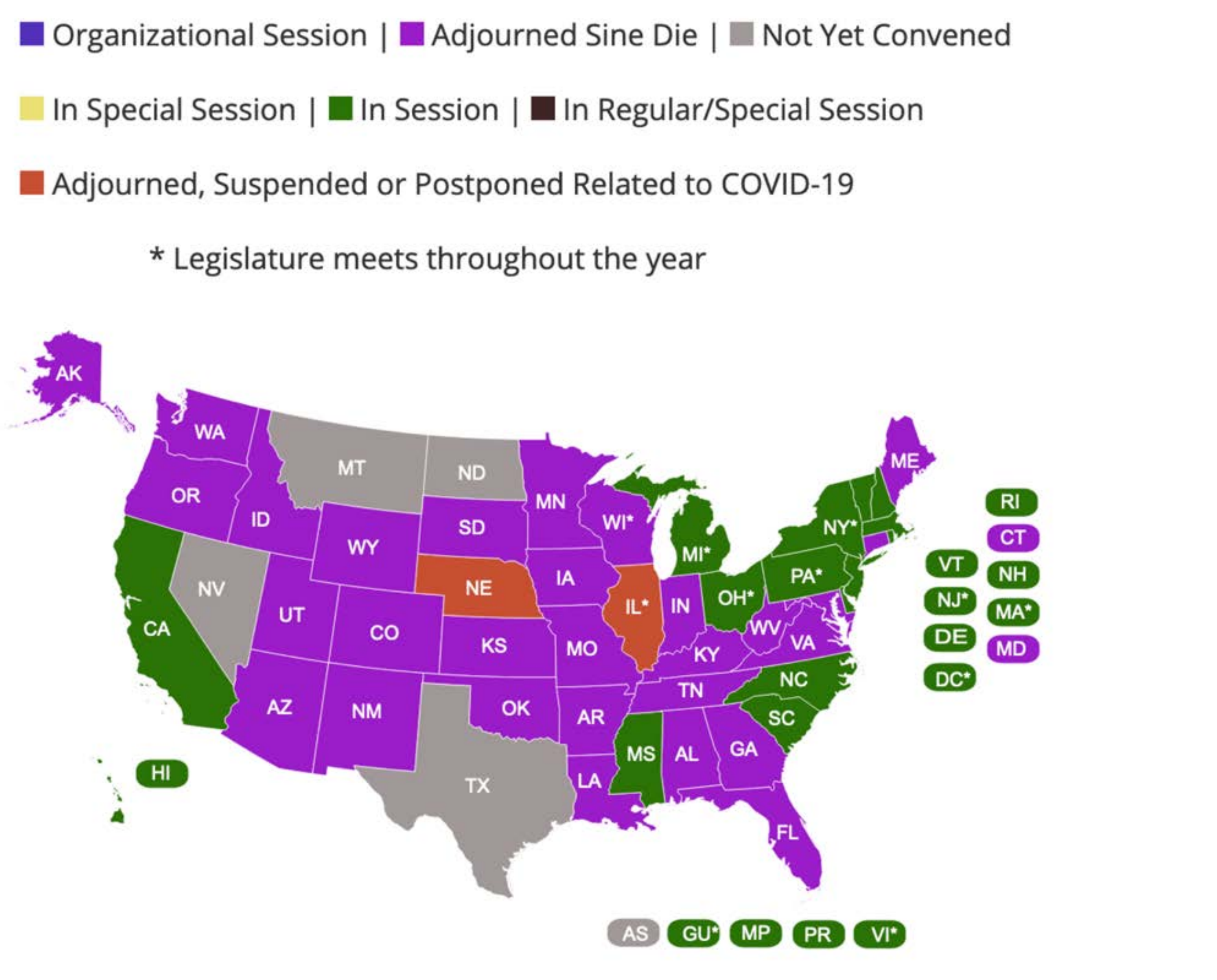
Other States

- Few states are in session right now
- Colorado (rolling state) passed a decoupling bill last month



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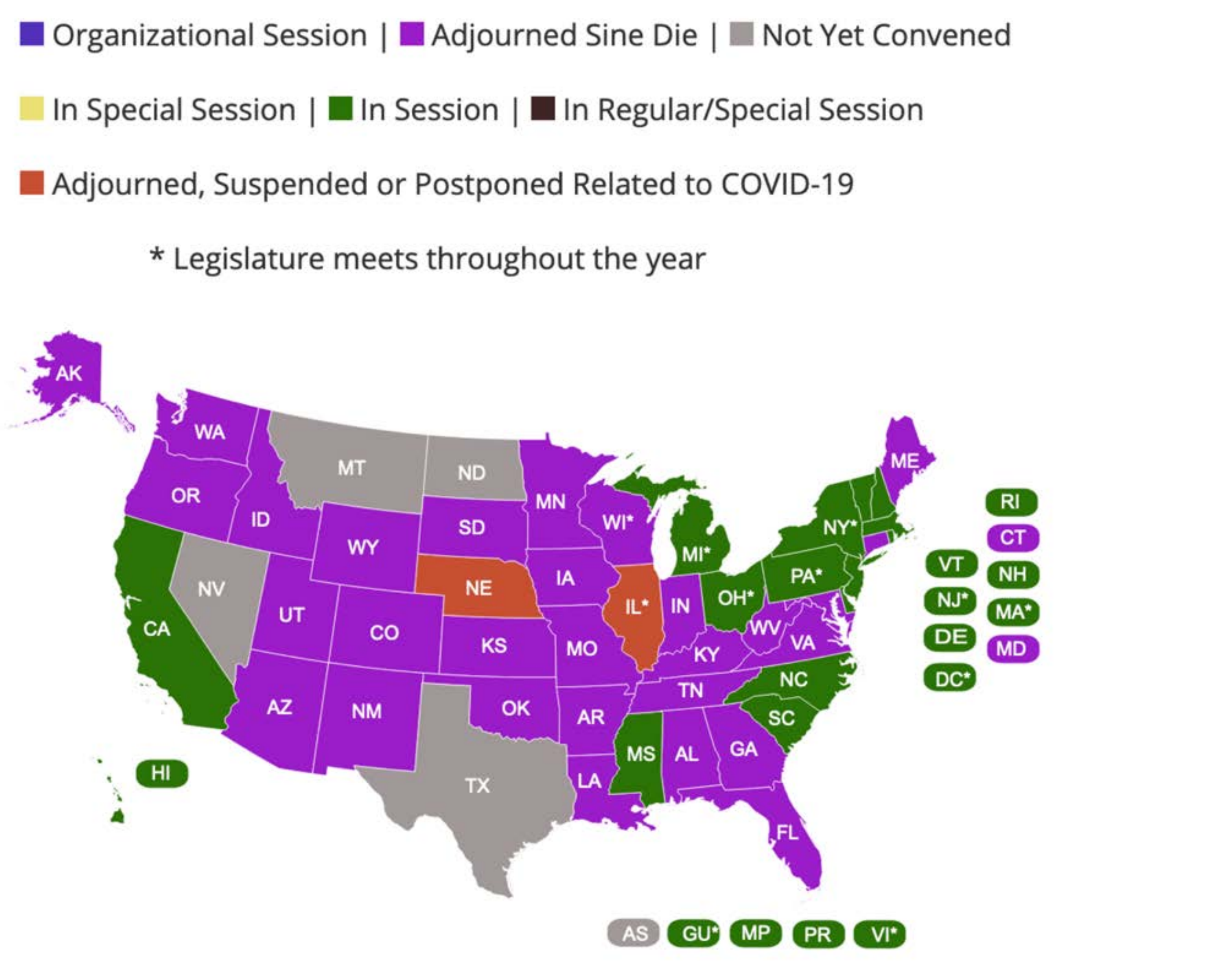
Other States

- Of the **static** states, unaware of any that have updated and conformed
  - But GA and NC have updated their dates and decoupled



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Recommendation

- Decouple from the changes to maintain status quo
- Consider whether individual changes make sense for Nebraska on our own schedule and with greater knowledge of need.

What about need?

- Impacted taxpayers will still get the much larger federal tax benefits

- The CARES Act provided billions of dollars of federal aid to Nebraska businesses and individuals who were impacted by the pandemic

- Non-targeted tax cuts have to be funded from some pool of resources

Questions?