

# Tax Cuts and Jobs Act of 2017 – An Update

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LEGISLATIVE REVENUE OFFICE

JANUARY 2018

# Presentation Outline

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## Summary of Provisions

### Individual Provisions

- Tax rates
- Deductions
- Other
- Preliminary revenue impacts

### Business Provisions

- Reductions, offsets, and preliminary impacts
- International

### Oregon Impact Details

### Potential Responses

# Summary of Provisions

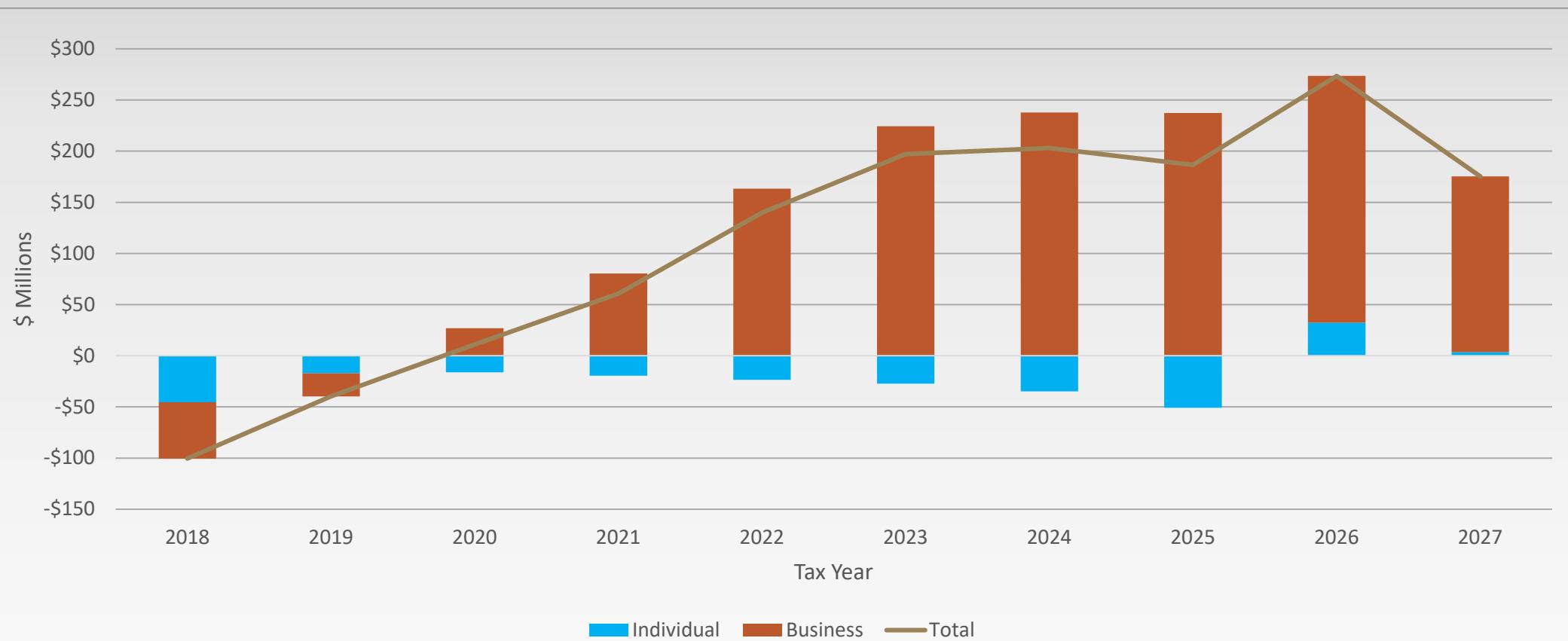
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A total of roughly 115 provisions in 3 categories:

- 30 Individual (includes pass-through deduction), generally tax years 2018 - 2025
- 65 business, generally tax years 2018+
- 20 international, generally tax years 2018+

| Individuals             |             |            | Businesses            |             |            | International      |             |            |
|-------------------------|-------------|------------|-----------------------|-------------|------------|--------------------|-------------|------------|
| Policy                  | Federal Tax | Oregon Tax | Policy                | Federal Tax | Oregon Tax | Policy             | Federal Tax | Oregon Tax |
| Tax rates               | -           | +          | Tax rates             | -           |            | Repatriation       | +           |            |
| Personal exemption      | +           | -          | Interest deduction    | +           | +          |                    |             |            |
| Standard deduction      | -           | +          | NOLs                  | +           | +          | Territorial System |             |            |
| Itemized deductions     | +           | +          | R&D amortization      | +           | +          |                    |             |            |
| Modify the AMT          | -           | +          | Bonus Depreciation    | -           | -          |                    |             |            |
| Child/ Dependent credit | -           | +          | AMT repeal            | -           | -          |                    |             |            |
| PTE deduction           | -           | -          | Deduction limitations | +           | +          |                    |             |            |
| Inflation adjustment    | +           | -          |                       |             |            |                    |             |            |

# Preliminary Oregon Revenue Impact\*, \$M



\*Excludes international provisions

# Individual Provisions

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LAW CHANGES THAT AFFECT ONLY THE PERSONAL INCOME TAX

# In Simplest Terms.....

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Income tax is calculated as follows:

Gross income – deductions = taxable income

Taxable income x tax rates = gross tax

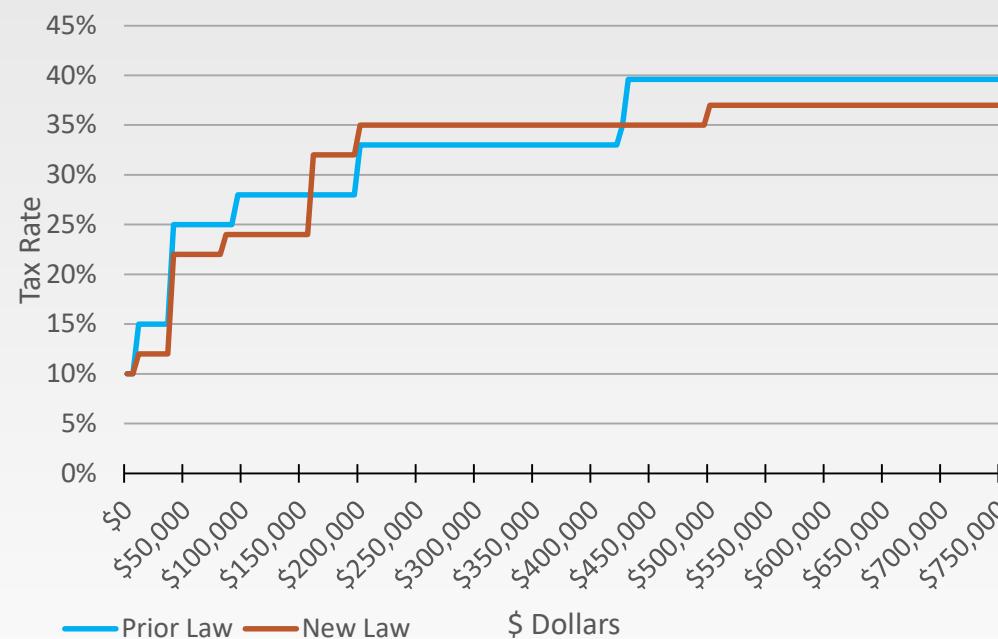
Gross tax – credits = tax

Congress changed deductions, tax rates, and credits

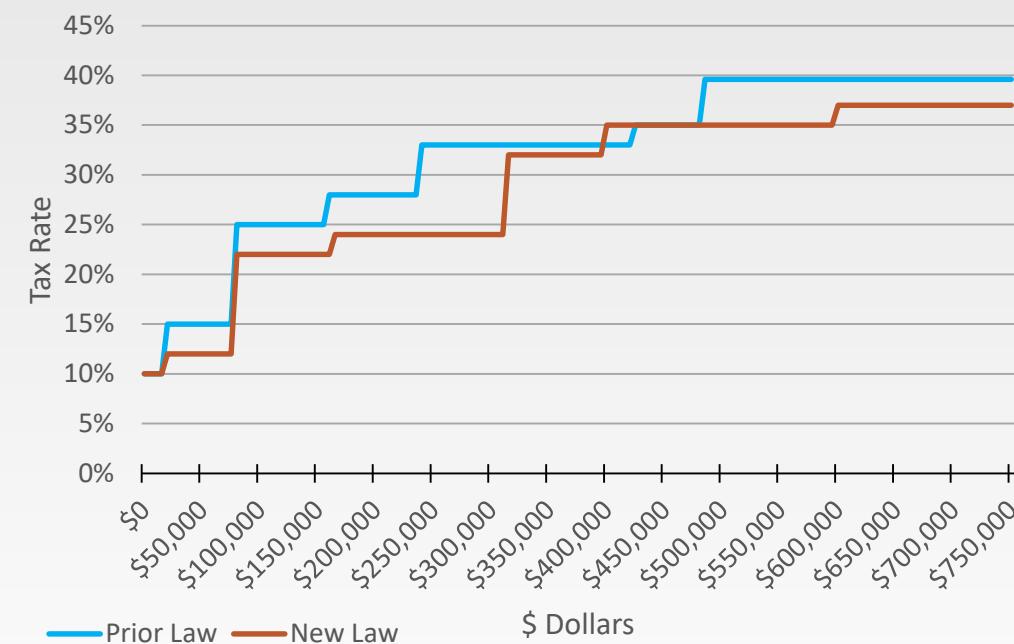
Deduction changes have the biggest impact on Oregon taxes

# Federal Tax Rates

SINGLE



JOINT



# Deductions

## PRIOR LAW

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### Personal Exemption

- \$4,150 per person

### Larger of:

- Standard Deduction
  - \$6,500 (single)
  - \$13,000 (joint)
- Itemized Deductions
  - SALT
  - Home mortgage interest
  - Charitable contributions
  - Pease limitation

## NEW LAW

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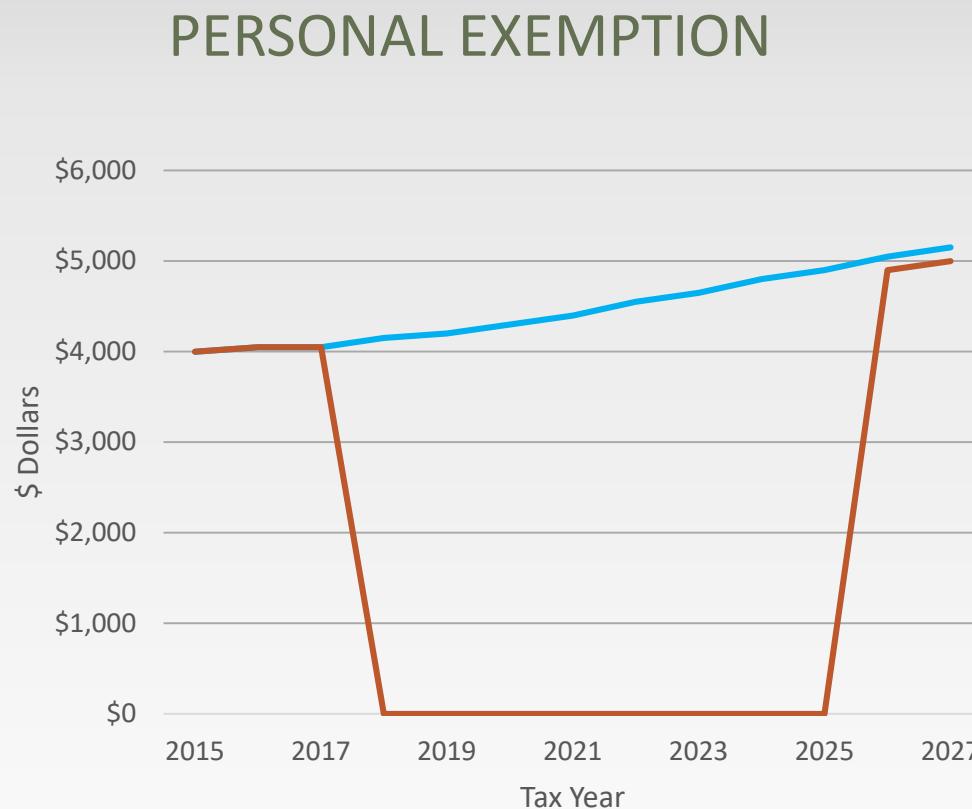
### No Personal Exemption

### Pass-Through Entity Income

### Larger of:

- Standard Deduction
  - \$12,000 (single)
  - \$24,000 (joint)
- Itemized Deductions
  - \$10,000 cap for income + property
  - Repeal of Pease limitation
  - Other

# Deductions That Were Reduced



## ITEMIZED DEDUCTIONS

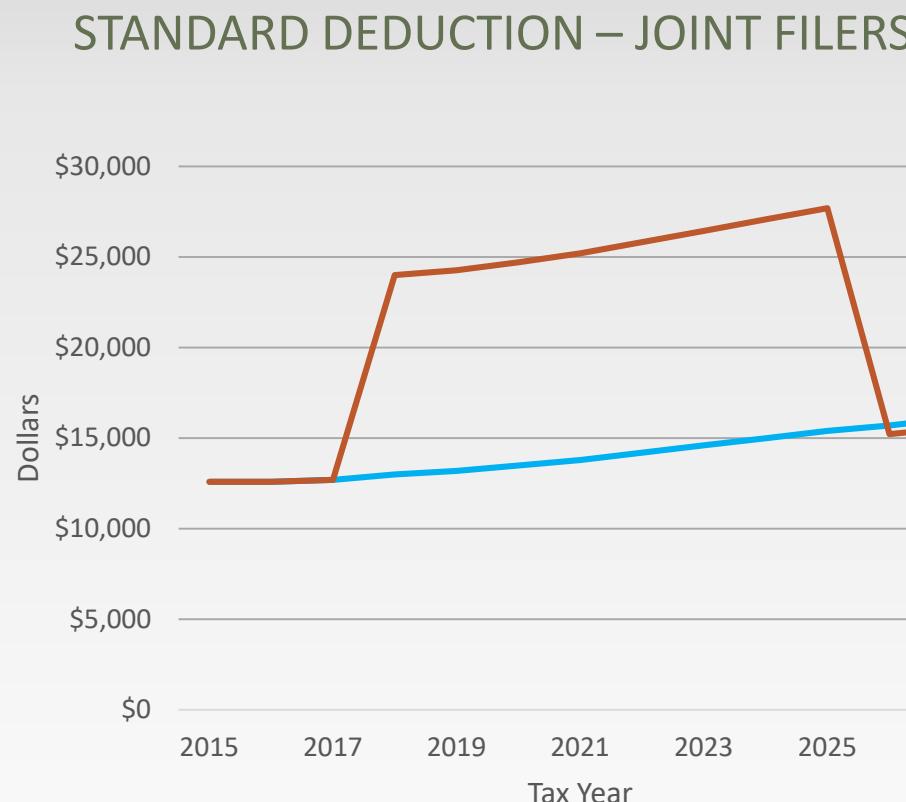
Income + property taxes limited to \$10,000

Home equity and some mortgage debt

Disallowed:

- Casualty losses
- Miscellaneous above 2% of AGI
- Unreimbursed business expenses
- Tax preparation fees
- Amounts paid to produce or collect taxable income

# Deductions That Were Increased



## PEASE LIMITATION REPEAL

Home mortgage interest

Charitable contributions

## PASS-THROUGH DEDUCTION

20% of “qualified business income”

Unlimited if income is below \$315,000 (J) or \$157,500 (S); phase-out over \$100K/\$50K

Limitation applies to “specified service businesses”, such as health, law, consulting

Deduction limited by wages paid, capital outlay

# Other Changes

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## Child and Dependent Tax Credit

- For qualifying children, increased from \$1,000 to \$2,000
- For other dependents, a new credit of \$500

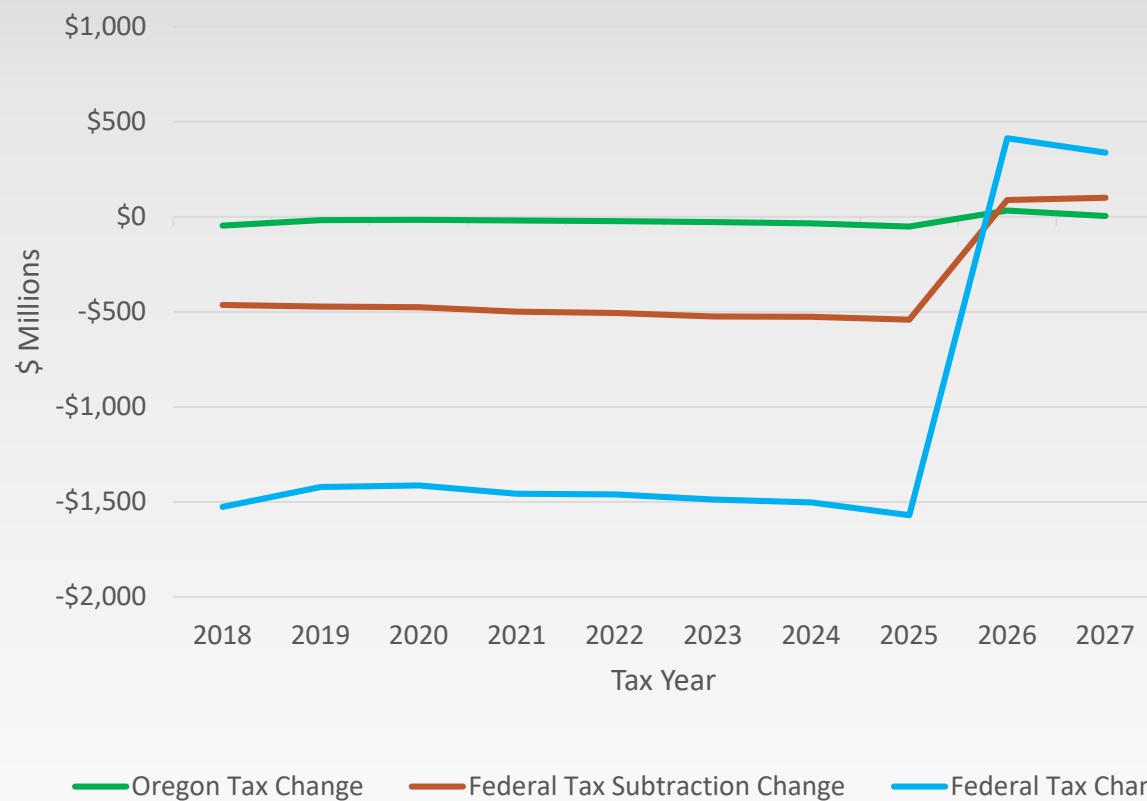
## AMT

- Exemption increased
- Phase-out threshold increased

## Inflation Factor (permanent)

- Chained CPI results in a slower pace of price changes due to consumer choices

# Preliminary Impacts of Individual Provisions



|                         | <b>Average Changes, \$M</b> |                |
|-------------------------|-----------------------------|----------------|
|                         | <u>2018-25</u>              | <u>2026-27</u> |
| Oregon Taxes            | -\$29                       | \$18           |
| Federal Tax Subtraction | -\$501                      | \$94           |
| Federal Taxes           | -\$1,480                    | \$375          |

# Business Provisions

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LAW CHANGES THAT AFFECT BOTH THE PERSONAL AND CORPORATE  
INCOME TAXES

# Business Tax Reductions

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21% C-corporation tax rate

Bonus Depreciation

- Increases from 50% to 100% through 2022, then phase-down to 20% in 2026, sunset in 2027

Repeal of AMT

Small Business Accounting

- Greater access to cash accounting

Section 179 Expensing

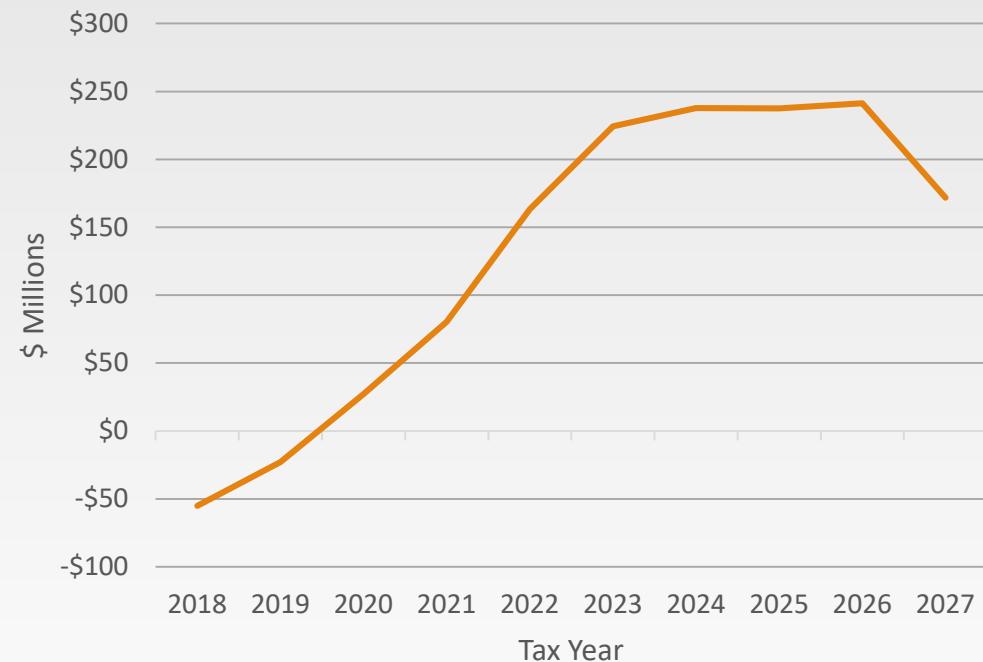
- Max increased from \$500,000 to \$1 million
- Phase-out threshold increased from \$2 million to \$2.5 million

# Business Tax Offsets and Impact

## INCREASES

- Limits net interest deduction
- Limits net operating losses
  - Oregon impact is on non-C-corps
- R&D amortization
  - Starts in 2023
- Domestic production
- Deduction limitations

## PRELIMINARY OREGON IMPACT



# International Taxation

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## Move from Worldwide System to Territorial System

- Changes focus from business residency to location of production
- Interaction with Oregon's tax haven law

## Key Features of Participation Exemption System

- Deduction for dividends received by a domestic corporation from certain foreign corporations
- Tax on global intangible low-taxed income (GILTI)
- Base erosion and anti-abuse tax (i.e. a kind of minimum tax)

## Repatriation

- Transition policy for changing systems
- Applies to undistributed, non-taxed foreign earnings since 1986
- Assets are taxed at 15.5% if liquid and 8% if illiquid
- Estimated federal revenue impact is roughly neutral except for repatriation dollars

# Oregon Impact Details

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# Oregon Full-Year Filers

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## Tax Increase or Decrease

- Federal taxes: 70% decrease, 10% increase, 20% no change
- Oregon taxes: 30% decrease, 40% increase, 30% no change

## Itemizers

- Share who itemize their federal taxes: 40% to 15%
- Share who itemize their Oregon taxes: remains at roughly 47%

# Preliminary Oregon Revenue Impacts, \$M

|                           | Tax Year |        |        |        |        |        |        |        |       |       |
|---------------------------|----------|--------|--------|--------|--------|--------|--------|--------|-------|-------|
|                           | 2018     | 2019   | 2020   | 2021   | 2022   | 2023   | 2024   | 2025   | 2026  | 2027  |
| <u>Individual</u>         |          |        |        |        |        |        |        |        |       |       |
| Property Taxes            | \$15     | \$16   | \$18   | \$20   | \$21   | \$23   | \$25   | \$28   | \$0   | \$0   |
| Miscellaneous             | \$83     | \$87   | \$92   | \$96   | \$101  | \$106  | \$111  | \$117  | \$0   | \$0   |
| Pass-thru                 | -\$182   | -\$192 | -\$205 | -\$218 | -\$231 | -\$244 | -\$260 | -\$277 | \$0   | \$0   |
| All Other                 | \$39     | \$72   | \$79   | \$82   | \$86   | \$88   | \$88   | \$81   | \$32  | \$4   |
| Subtotal                  | -\$45    | -\$17  | -\$16  | -\$20  | -\$23  | -\$27  | -\$35  | -\$51  | \$32  | \$4   |
| <u>Businesses</u>         |          |        |        |        |        |        |        |        |       |       |
| Bonus Depreciation        | -\$76    | -\$77  | -\$57  | -\$36  | -\$25  | -\$11  | \$6    | \$19   | \$27  | \$23  |
| Section 179 Expensing     | -\$12    | -\$15  | -\$10  | -\$6   | -\$5   | -\$4   | -\$3   | -\$2   | -\$2  | -\$2  |
| Small Business Accounting | -\$22    | -\$20  | -\$11  | -\$7   | -\$5   | -\$5   | -\$5   | -\$5   | -\$5  | -\$4  |
| Net Interest              | \$29     | \$46   | \$55   | \$58   | \$71   | \$82   | \$85   | \$90   | \$98  | \$77  |
| Net Operating Losses      | \$6      | \$9    | \$11   | \$15   | \$23   | \$30   | \$31   | \$27   | \$19  | \$9   |
| R&D                       | \$0      | \$0    | \$0    | \$13   | \$60   | \$84   | \$73   | \$53   | \$33  | \$16  |
| All Other                 | \$20     | \$33   | \$40   | \$43   | \$45   | \$47   | \$49   | \$56   | \$71  | \$52  |
| Subtotal                  | -\$55    | -\$23  | \$27   | \$80   | \$163  | \$224  | \$238  | \$237  | \$241 | \$172 |

# Individual Tax Examples, Single Filer

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|                |                    | Old      | New      | Difference | Old       | New       | Difference |  |
|----------------|--------------------|----------|----------|------------|-----------|-----------|------------|--|
|                |                    | AGI      | \$50,000 | \$50,000   |           | \$180,000 | \$180,000  |  |
| <u>Federal</u> | Personal Exemption | \$4,150  | \$0      | -\$4,150   | \$4,150   | \$0       | -\$4,150   |  |
|                | S/I Deduction      | \$6,500  | \$12,000 | \$5,500    | \$33,500  | \$20,000  | -\$13,500  |  |
|                | Taxable Income     | \$39,350 | \$38,000 | -\$1,350   | \$142,350 | \$160,000 | \$17,650   |  |
|                | Tax                | \$5,491  | \$4,370  | -\$1,121   | \$32,701  | \$32,890  | \$189      |  |
|                |                    |          |          |            |           |           |            |  |
|                |                    |          |          |            |           |           |            |  |
| <u>Oregon</u>  | Deductions         | \$2,215  | \$2,215  | \$0        | \$19,000  | \$19,000  | \$0        |  |
|                | Fed Tax Subt       | \$3,325  | \$3,325  | \$0        | \$0       | \$0       | \$0        |  |
|                | Taxable Income     | \$44,460 | \$44,460 | \$0        | \$161,000 | \$161,000 | \$0        |  |
|                | Tax                | \$3,557  | \$3,557  | \$0        | \$14,571  | \$14,571  | \$0        |  |

# Individual Tax Examples, Joint Filer

|                |                    | Family of Four |          |            | No Children, With/Without Pass-Through Income |           |            |           |           |            |
|----------------|--------------------|----------------|----------|------------|-----------------------------------------------|-----------|------------|-----------|-----------|------------|
|                |                    | Prior          | New      | Difference | Prior                                         | New       | Difference | Prior     | New       | Difference |
|                |                    | AGI            | \$75,000 | \$75,000   | \$400,000                                     | \$400,000 |            | \$400,000 | \$400,000 |            |
| <u>Federal</u> | Personal Exemption | \$16,600       | \$0      | -\$16,600  | \$2,988                                       | \$0       | -\$2,988   | \$2,988   | \$0       | -\$2,988   |
|                | S/I Deduction      | \$19,400       | \$24,000 | \$4,600    | \$56,600                                      | \$25,000  | -\$31,600  | \$56,600  | \$105,000 | \$48,400   |
|                | Taxable Income     | \$39,000       | \$51,000 | \$12,000   | \$340,412                                     | \$375,000 | \$34,588   | \$340,412 | \$295,000 | -\$45,412  |
|                | Child Credit       | \$2,000        | \$4,000  | \$2,000    | \$0                                           | \$0       | \$0        | \$0       | \$0       | \$0        |
|                | Tax                | \$2,898        | \$1,739  | -\$1,159   | \$87,061                                      | \$83,379  | -\$3,682   | \$87,061  | \$59,379  | -\$27,682  |
|                |                    |                |          | -40.0%     |                                               |           | -4.2%      |           |           | -31.8%     |
| <u>Oregon</u>  | Deductions         | \$15,500       | \$15,500 | \$0        | \$23,024                                      | \$24,000  | \$976      | \$23,024  | \$104,000 | \$80,976   |
|                | Fed Tax Subt       | \$2,898        | \$1,739  | -\$1,159   | \$0                                           | \$0       | \$0        | \$0       | \$0       | \$0        |
|                | Taxable Income     | \$56,602       | \$57,761 | \$1,159    | \$376,976                                     | \$376,000 | -\$976     | \$376,976 | \$296,000 | -\$80,976  |
|                | Tax                | \$3,804        | \$3,908  | \$104      | \$34,585                                      | \$34,488  | -\$97      | \$34,585  | \$26,568  | -\$8,017   |

# Potential Responses

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## Public Sector

- Disconnect from certain provisions
  - Pass-through entity deduction (or a direct tax)
  - Bonus depreciation
  - Section 179 expensing
- Change funding sources
  - Convert state income tax dollars to charitable contributions
  - Increase payroll taxes and decrease income taxes

## Private Sector

- Employee becomes independent contractor
- Recharacterize certain pass-through income to eligible sector
- Set up a C-corporation to receive income