



District of Columbia



State Revenue Implications of Federal Tax Reform

Keith Richardson
Deputy Chief Financial Officer District of
Columbia
Office of Tax and Revenue

March 23, 2018



District of Columbia

Tax Changes Under the TCJA

- ❑ The Tax Cuts and Jobs Act (TCJA) is the most significant revision to the federal tax system since 1986
- ❑ TCJA makes substantial changes to the Internal Revenue Code that impact both the federal and District tax liabilities of District taxpayers
 - *An estimated **83%** of District taxpayers will **experience a decrease or experience no change** in their combined net federal and District income taxes*
 - *An estimated **17%** of District taxpayers will **experience an increase** in their combined net federal and District income taxes*
- ❑ The changes to individual income tax and estate tax are temporary and will expire after December 31, 2025
- ❑ The changes to the corporate income tax are permanent



District of Columbia

Major Provisions



District of Columbia

Federal Rate and AMT Changes

Federal Individual and Corporate tax rates reduced and AMT Adjusted

- Individual income tax rates were reduced for most federal income tax brackets
 - Alternative minimum tax (AMT) exemption and phaseout levels were substantially increased
 - Corporate income tax rates were changed from a graduated structure to a flat 21%
- **Federal Effect:**
- Reduces federal tax liability for most individual taxpayers and corporations
 - Offsets, at least in part, the limitation of SALT deduction for individuals and elimination of other deductions
- **District Effect:**
- No impact on District revenues
 - No impact on District taxpayers' District income or franchise tax liability



District of Columbia

District Coupling With Major Federal Tax Provisions

- **Beginning January 1, 2018 the District Coupled to the Federal Amounts:**
 - Standard Deduction – D.C. Code Ann. § 47-1801.04(44)(A)(iv)
 - Personal Exemption - D.C. Code Ann. § 47-1806.02(i)(2)
 - Estate Tax Basic Exclusion Amount - D.C. Code Ann. § 47-3701(4)(C)



District of Columbia

Changes to DC Standard Deduction and Personal Exemption

	2016	2017	2018 pre-TCJA	2018 TCJA
Standard Deduction				
Single	\$5,200	\$5,650	\$6,500	\$12,000
Married	\$8,350	\$10,275	\$13,000	\$24,000
Head of Household	\$6,500	\$7,800	\$9,350	\$18,000
Personal exemption	\$1,775	\$1,775	\$4,150	\$0



District of Columbia

Standard Deduction

Federal standard deduction almost doubled

(2018 - Married: \$24,000, Single: \$12,000, Head-of-Household: \$18,000)

- ❑ **Federal Effect:** Reduces federal taxable income for taxpayers who:
 - Currently claim the standard deduction
 - Previously claimed itemized deductions less than the new higher standard deduction

- ❑ **District Effect:** Reduces District taxable income for taxpayers who:
 - Currently claim the standard deduction (*59% of all District taxpayers*)
 - Previously claimed itemized deductions that are less than the new higher standard deduction (*13% of all District taxpayers*)



District of Columbia

Personal Exemption

Personal Exemption Suspended

(\$4,150 per exemption before TCJA)

❑ **Federal Effect:**

- Increases federal taxable income for some District taxpayers (especially those with dependents)
- Largely offset by increase to the standard deduction and federal child tax credit

❑ **District Effect:**

- Increases District taxable income for some District taxpayers (especially those with dependents)



District of Columbia

Child Tax Credit

The Federal Child Tax Credit Increased

- \$2,000 per child
- Partial credit for certain non-child dependents
- Income thresholds increased
- \$1,400 is refundable

□ Federal Effect:

- Decreases federal tax liability for eligible taxpayers
- Partially offsets suspension of the personal exemption for eligible taxpayers with dependents

□ District Effect:

- The District does not have a child tax credit
- District taxpayers with dependents will not be able to reduce their District taxable income with a child tax credit or a personal exemption



District of Columbia

SALT Deduction Limitation

Federal deduction for state and local taxes, including property tax, is limited to \$10,000

❑ **Federal Effect:**

- No impact on federal taxable income for taxpayers who claim the standard deduction
- Increases federal taxable income of taxpayers who itemize deductions and pay more than \$10,000 in state and local taxes. For 3% of taxpayers, the SALT limitation increases federal tax despite other offsetting tax code changes.

❑ **District Effect:**

- No impact on District taxpayers who claim the standard deduction
- No impact on District taxable income for District taxpayers who itemize deductions:
 - District income taxes are not deductible from District taxable income
 - The federal deduction limitation to property taxes does not apply to District taxes (District tax form will be modified to ensure full deduction)



District of Columbia

Estate Tax Basic Exclusion Amount Increased

Increases the Estate Tax Basic Exclusion Amount from \$5 million to \$10 million (adjusted for inflation to \$5.6 million and to \$11.2 million for 2018)

❑ **Federal Effect:**

- Reduces the number of estates required to file a federal estate tax return
- Eliminates the federal estate tax liability for taxable estates up to \$11.18 million
- Decreases the federal estate tax liability for taxable estates over \$11.18 million

❑ **District Effect:**

- Reduces the number of estates required to file a District estate tax return
- Eliminates the District estate tax liability for taxable estates up to \$11.18 million
- Decreases the District estate tax liability for taxable estates over \$11.18 million



District of Columbia

BUSINESS TAX CHANGES

- Federal corporate tax decrease for District businesses of an estimated \$460 million in 2019, mostly from federal rate reduction and repeal of corporate AMT
 - Corporate rate reductions do not change District taxes
 - District does not conform to federal AMT so no impact
- Passthrough (sole proprietor and partnerships) business income deduction reduces federal taxable individual income
- Business expensing provisions that allow the immediate deduction of investment costs will reduce federal tax revenue in 2018 and 2019. The District does not conform to the federal change in expensing



District of Columbia

BUSINESS TAX CHANGES

- Most of positive fiscal impact offset after 2022 is from expanding the taxable income base
 - Limitation on use of net operating losses
 - Limitation on deduction of interest expense
- Tax on foreign income increases federal revenue by \$146 million in 2019 on District taxpayers, offsetting some of the federal corporate tax reduction and will increase the amount of funds available for investment and dividends in the District



District of Columbia

20% Deduction for Qualified Business Income

Creates a new deduction for business owners for 20% of income received from certain qualified businesses and passthrough entities

❑ **Federal Effect:**

- Allows taxpayers to deduct 20% of “qualified business income” on their individual income tax returns
- Intended to provide business owners a benefit similar to the lowering of corporate rate

❑ **District Effect:**

- District taxable income not affected



District of Columbia

Immediate Expensing/Interest Deduction Limitation

Immediate Expensing Deduction Allowed

Allows businesses to immediately deduct the purchase of an asset as an expense instead of depreciating the asset over time

□ **Federal Effect:**

- Accelerates tax benefit to businesses that purchase assets
- Decreases federal tax liability

□ **District Effect:**

- The District previously decoupled from this provision
- No impact on District tax liability

Interest Deduction Limited

Limits the deduction for interest paid by businesses

□ **Federal Effect:**

- Limits ability of businesses to deduct interest
- Increases federal tax liability
- Intended to offset the effect of immediate expensing deduction

□ **District Effect:**

- The District is coupled with federal law regarding the deductibility of interest and, therefore, will follow this new limitation
- Increases District tax liability



District of Columbia

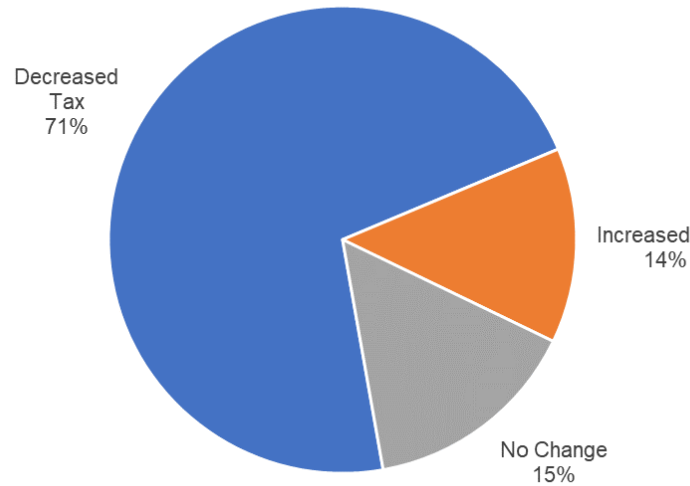
Individual Income Tax Effects



District of Columbia

Federal and DC Tax Impact

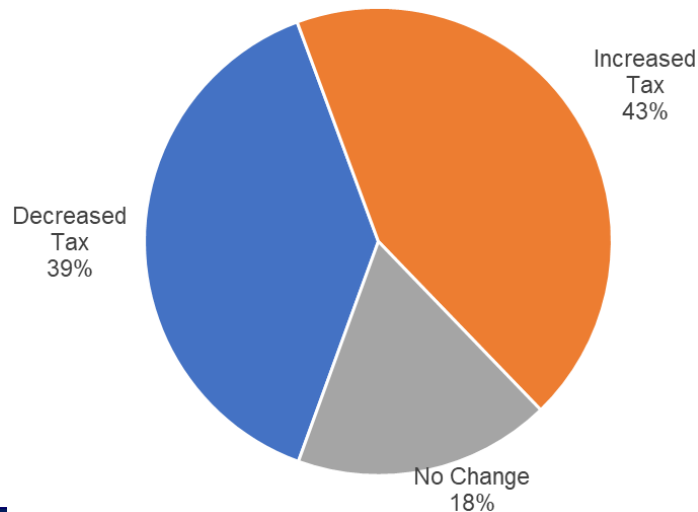
Federal Tax Impact



- Federal tax revenue decreases \$617.3 million

	Federal			Net
	Increase	Decrease	No Change	
% of returns with change	14%	71%	15%	100%
Federal Change (millions)	\$109.1 M	-\$726.4 M		-\$617.3 M
Median change (dollars per return)	\$815	-\$1,206		

DC Tax Impact



- DC tax revenue increases \$56.4 million

	DC			Net
	Increase	Decrease	No Change	
% of returns with change	43%	39%	18%	100%
District Change (millions)	\$82.3 M	-\$25.9 M		\$56.4 M
Median change	\$336	-\$88		

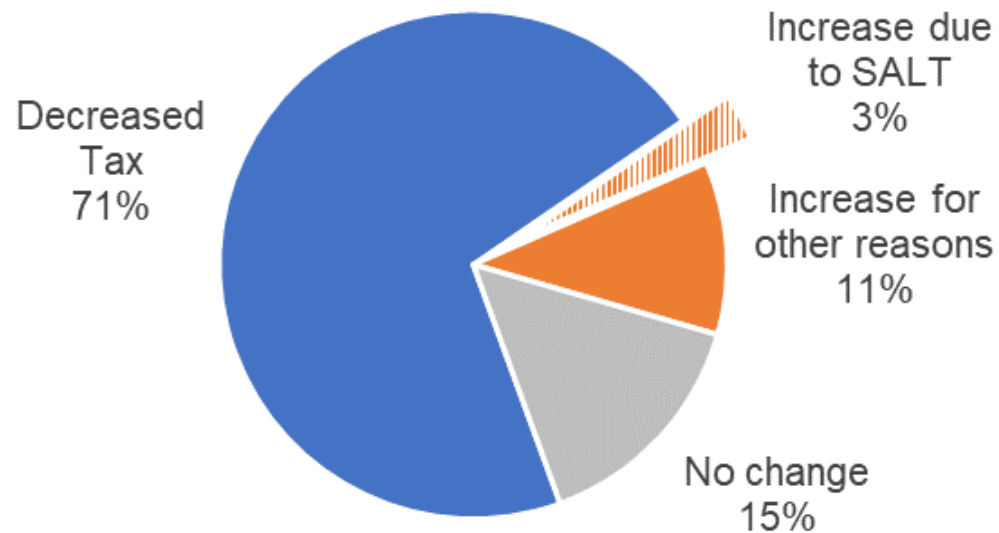


District of Columbia

Who is affected by SALT Limitation

- 3% (11,310) of District taxpayers with federal tax increase because the SALT limitation is not offset by other tax changes.

Federal Tax Change





District of Columbia

SUMMARY



District of Columbia

Summary of Tax Impact

Federal

- Most DC Residents' federal tax reduced
 - 83% tax reduction or no change
 - Median federal income tax cut \$1,206
- Some see increased federal tax
 - 17% tax increase
 - Lower tax rate and higher standard deduction does not offset limited itemized deductions and suspension of personal exemption for this group

DC

- Many DC residents see DC tax increase
 - 57% tax decrease or no change
 - 43% tax increase
 - Mostly taxpayers with income between \$50,000 and \$200,000
 - Suspension of personal exemption is not offset by child tax credit or lower rates as with federal tax
 - Median increase \$336



District of Columbia

Summary for DC

- ❑ Effective tax rate increases from 4.8% to 4.9% (tax as share of income)
 - ❑ Higher increase for lower income taxpayers
- ❑ Federal tax changes will result in \$51.9 million additional DC tax revenue in FY 2019
 - ❑ \$56.4 million individual income tax revenue
 - ❑ \$2 million business franchise tax revenue
 - ❑ Doubling of estate tax threshold reduces DC revenue by \$6.5 million
- ❑ Major uncertainties remain
 - ❑ Repatriated income impact on District economy and finances unclear