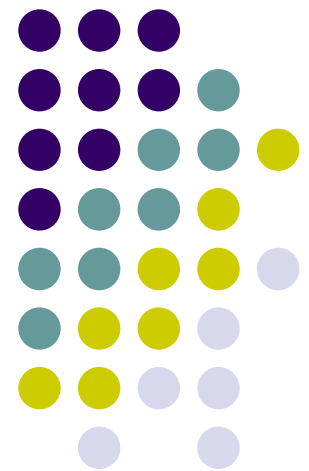


# State Income Tax Conformity

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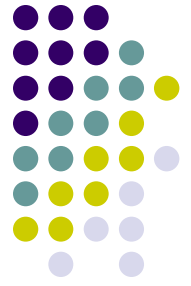
Interim Revenue and  
Transportation Committee  
Montana Legislature  
December 7, 2007





# Outline

- Reasons for conformity
- Implications of conformity
- Current status of conformity
- Issues in conformity
- Questions and answers



# Conformity - Defined

- Defining elements of state income tax by reference to IRC
- Aspects defined by reference
  - Tax base
  - Itemized deductions
  - Specific provisions
- Automatic/Rolling - Tied to IRC on an ongoing basis
- Fixed date -- Tied to IRC as of specific date



# Reasons for Conformity

- Taxpayer convenience, improved compliance
  - No need for dual accounts, tracking two sets of rules, etc.
- Simplified administration and enforcement
  - Rely on federal infrastructure for rules, definitions, etc.
  - Use exchanges of information from federal government for state enforcement
- Are, for the large part, trying to define same concept -- economic income



# Implications of Conformity

- Conformity necessarily involves some ceding of control over the state's tax policy
  - Actions of federal government affect state tax policy
  - Actions of federal government affect state revenue flows and budget situation
- Non-conformity increases 'relative' complexity for all parties
  - Greatest additional burdens fall on taxpayers



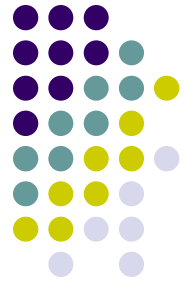
# Status of Conformity

- 41 states plus D.C. have broad-based income tax
  - All but five -- AL, AR, MS, NJ, PA -- conform to federal base
- Starting points
  - Twenty-eight begin with AGI
  - Nine -- CO, ID, MN, NC, ND, OR, SC, UT, VT -- begin with federal taxable income
- Eighteen States with fixed-date conformity



# Itemized Deductions

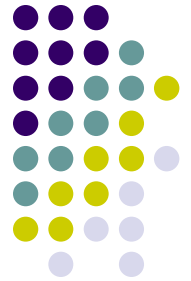
- Thirty-three allow itemized deductions
  - 16 follow federal deduction for non-income taxes
  - 29 follow interest expense deduction
  - 24 follow medical expense deduction
  - 27 follow charitable contribution deduction
  - 20 follow miscellaneous and other deductions



# Recent Provisions

- Nineteen do not conform to Sec. 199 ‘manufacturing deduction’
- Only 13 conformed to the initial ‘bonus depreciation’ provisions; 25 non-conformed; 9 hybrid approaches
- Eighteen states decoupled from Se. 179 Small Business Expensing provisions
- Eighteen States retain some form of estate tax
- Please treat numbers as approximate.

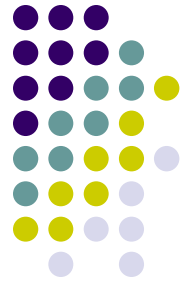




# Issues in Conformity

- Rolling vs. Fixed Date
  - ‘Rolling’ changes the question from “Shall we conform?” to “Shall we non-conform?”
  - Issue of delegating legislative authority
- Degree of Conformity
  - Base -- AGI, Taxable Income, Tax Liability
    - Movement away from “piggyback” taxes
  - Itemized Deductions
  - Balance of administrative ease/policy control

# Assessing Discrete Provisions



- Degree of complexity varies significantly based on type of provision
  - Issues with “one-time” consequences are manageable
    - Sec. 199 manufacturing deduction
    - Special case of ‘corporate incentives’
  - Issues involving ‘timing’ create significant complexity
    - Depreciation
    - Deferred income/tax
  - Information availability is critical



# Conclusion

- Overall, conformity contributes to the administration of the tax system
- Has positive/negative features
- Question of balancing need/desirability of control against issues of complexity and compliance that arise from non-conformity
  - What are the revenue/policy impacts?
  - What are the complexity impacts?
  - What are alternatives to non-conformity



Harley T. Duncan

Executive Director

Federation of Tax Administrators

Ph. 202/624-5891

<harley.duncan@taxadmin.org>