



PERSONAL INCOME TAX OVERVIEW

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Outline

- ▶ Structure
- ▶ Annual link up
- ▶ Definitions
- ▶ Recent changes

PIT: Structure

- **Tax Base:** taxable income
 - 32 V.S.A. § 5811(21)
- **Tax Rates:** progressive brackets, marginal tax rates
 - 32 V.S.A. § 5822
- **Tax Liability:** adjustments, tax credits
 - 32 V.S.A. ch. 151, subch. 2

PIT: Annual Link Up

- Statutes often incorporate other law from the same jurisdiction or from a different authority like the federal government through reference.
- Vermont income tax law incorporates federal income tax law by pinpointing the laws of the U.S. in effect at the end of a given year (Dec. 31). In practice, the year is generally updated annually.

PIT: Annual Link Up

32 V.S.A. § 5824 reads:

§ 5824. Adoption of federal income tax laws

The statutes of the United States relating to the federal income tax, as in effect on December 31, 2021, but without regard to federal income tax rates under 26 U.S.C. § 1, are hereby adopted for the purpose of computing the tax liability under this chapter and shall continue in effect as adopted until amended, repealed, or replaced by act of the General Assembly.

PIT: Annual Link Up

- The effective date of the bill amending 32 V.S.A. § 5824 applies the changes to a specific taxable year, and all following taxable years (until amended). For example, in 2022 Act 148 Sec. 9(c):
 - “Notwithstanding 1 V.S.A. § 214, Secs. 7 and 8 (annual link to federal statutes) shall take effect retroactively on January 1, 2022 and shall apply to taxable years beginning on and after January 1, 2021.”

PIT Definitions: Gross Income

- Under the federal Internal Revenue Code, “gross income means all income from whatever source derived”, with certain exclusions. 26 U.S.C. § 61; *Commissioner v. Glenshaw Glass*, 348 U.S. 426, 431-33 (1955) (income is any accession to wealth).
 - Examples
 - Included in gross income: wages, tips, salaries, commissions, rent, royalties, interest, dividends, IRA distributions, pensions and annuities, capital gains, and cancellation of debt
 - Excluded from gross income: certain Social Security income, interest on State or local bonds, cancellation of certain student loan debt

PIT Definitions: Adjusted Gross Income (AGI)

- Under federal law, the term “adjusted gross income” means gross income minus certain exclusions and deductions. 26 U.S.C. § 62; 32 V.S.A. § 5811(21).
 - Examples of common federal adjustments to gross income
 - Teacher expenses; IRA deductions; student loan interest; tuition and fees
 - Other adjustments
 - Certain business expenses of reservists, performing artists, and fee-basis government officials; health savings account contributions; moving expenses for Armed Forces; the deductible part of self-employment tax; self-employed SEP, SIMPLE, and qualified plans; self-employed health insurance; penalty on early withdrawal of savings; alimony paid

PIT Definitions: Taxable Income

- Federal taxable income is adjusted gross income minus itemized or standard and other miscellaneous deductions. 26 U.S.C. § 63.
- Vermont's personal income tax defines "taxable income" as "federal adjusted gross income determined without regard to 26 U.S.C. § 168(k)", relating to bonus depreciation, and adds backs certain income and subtracts other types of income. 32 V.S.A. § 5811(21).
- Vermont taxable income is different from federal taxable income. There are items of income that federal law and the U.S. Constitution prohibit states from taxing. Other than those pre-empted types of income, Vermont makes policy decisions to tax or exempt income.
 - Examples: railroad retirement income; discriminatory tax treatment of federal-source income in favor of state-source income.

Federal Income Tax Definitions ...

Federal tax return
(form 1040)

Gross Income

Wages, salaries, tips, dividends, capital gains, IRA/pensions, business income, etc.

minus

“Above the Line” Deductions

Examples: teacher expenses, student loan interest, self-employed plans, etc.

equals

Adjusted Gross Income

... Flow Through to Vermont

From federal
form 1040

Adjusted gross income

plus

Additions to adjusted gross income

Bonus depreciation, interest from non-Vermont state and local bonds

minus

Subtractions from adjusted gross income

Standard deduction*

\$6,350 for single filer,
\$12,700 for married filer

Personal exemptions*

\$4,350 for taxpayer,
spouse, and any
dependents

Other subtractions

- Interest income from U.S. bonds
- Capital gains exclusion
- Social Security exemption
- Medical expenses

equals

Vermont taxable income

*Amounts for tax year
2021; indexed annually
for inflation

PIT: Recent Changes to Tax Base

- Prior to 2002, Vermont's PIT tax base was a percentage of federal taxable income.
- In 2002, Act 140 amended the starting point for Vermont's PIT tax base to federal taxable income.
- In 2017, Act 53 changed the starting point for Vermont's PIT tax base to federal AGI.
- In 2018 (Spec. Sess.), Act 11 made further structural changes to Vermont's PIT tax base in direct response to the federal Tax Cuts and Jobs Act of 2017.

PIT: Recent Federal Changes, TCJA 2017

Federal Tax Cuts and Jobs Act, enacted Dec. 22, 2017

- Most significant federal PIT changes: elimination of personal exemptions, doubling of standard deduction, and alteration of numerous itemized and miscellaneous deductions.
 - Most were effective through TY 2025

Vermont's response

- “Decoupling” from many federal provisions, meaning Vermont tax code shifted to State-specific definitions and structure independent from federal tax code.
 - As a result, fewer federal income tax changes “flow through” to Vermont.

PIT: 2022 Vermont Legislative Session

H.738 (Act 179), an act relating to technical and administrative changes to Vermont's tax laws

- [As Enacted](#)
- [Act Summary](#)

H.510 (Act 138), an act relating to a Vermont Child Tax Credit and the Vermont Social Security income exclusion

- [As Enacted](#)
- [Act Summary](#)

PIT Recent VT Changes: Act 138 of 2022

- Refundable \$1,000 VT child tax credit for qualifying children 5 and under.
 - Phases out for taxpayers with AGI over \$125,000 (credit is \$0 at \$175,000 AGI).
- VT child and dependent care credit expanded to a refundable credit that is 72% of federal CDC credit.
- VT EITC expanded to 38% of federal EITC.
- New VT student loan interest deduction
 - Only for taxpayers with AGI \$120,000 or less (single filers) or \$200,00 or less (joint filers).
- Expands Social Security benefits exemption by \$5,000.
- Adds new \$10,000 retirement income exemptions.