

Governor's Tax Relief Package FY24

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Governor's Tax Relief Package

- Builds on the great work done last year in Act 138
- ~\$17 million in state tax reductions
- JFO estimated \$10-\$20 million in federal tax reductions
- These provisions are accounted for in the GovRec budget

Pass-Through Entity Tax/SALT Cap Workaround

- Proposal: Implement a Pass-Through Entity (PTE) Tax/SALT Cap Workaround allowable by IRS Notice 2020-74
 - Creates an optional pass-through entity tax that allows PTE businesses to deduct more than the Tax Cuts and Jobs Act's limit of \$10,000 in state and local taxes.
 - **If structured properly, reduces taxes for Vermonters while *gaining* state revenue**
- Current Vermont law: VT currently only allows this for non-residents and composite filers, creating a disadvantage for resident PTE owners.
- Revenue Impact
 - JFO estimates this as a \$10-\$20 million federal tax cut for Vermont business owners.
 - The Governor's recommended model of this policy is estimated to generate additional state base revenue of \$500,000

No Pass-Through Entity Tax

- \$1 million in S-Corp income
- \$0 PTE tax paid
- \$1 million Federal K1 distribution
- SALT Deduction Cap of \$10,000

~\$300,000 paid in federal taxes

~\$80,000 paid in state taxes

Pass-Through Entity Tax

- \$1 million in S-Corp income
- \$76,000 PTE tax paid
- PTE tax fully deductible at entity level
- \$924,000 Federal K1 distribution

~\$275,000 paid in federal taxes (Savings = \$25,000)

~\$73,000 paid in state taxes (Savings = \$7,000)

Problem

State loses \$7,000 from this taxpayer if we give them a full credit for pass-through entity taxes paid.



Solution

Offer a Personal Income Tax credit of 90 cents for each \$1 of pass-through entity taxes paid.

Pass-Through Entity Tax

- \$1 million in S-Corpincome
- \$76,000 in PTE tax
- \$924,000 Federal K1 distribution
- \$68,400 credit for PTE taxes paid
- About \$275,000 paid in federal taxes
 - Federal savings of \$25,000
- About \$81,000 paid in state taxes
 - State taxes increase ~\$1,000
- Taxpayer still makes the election due to federal savings

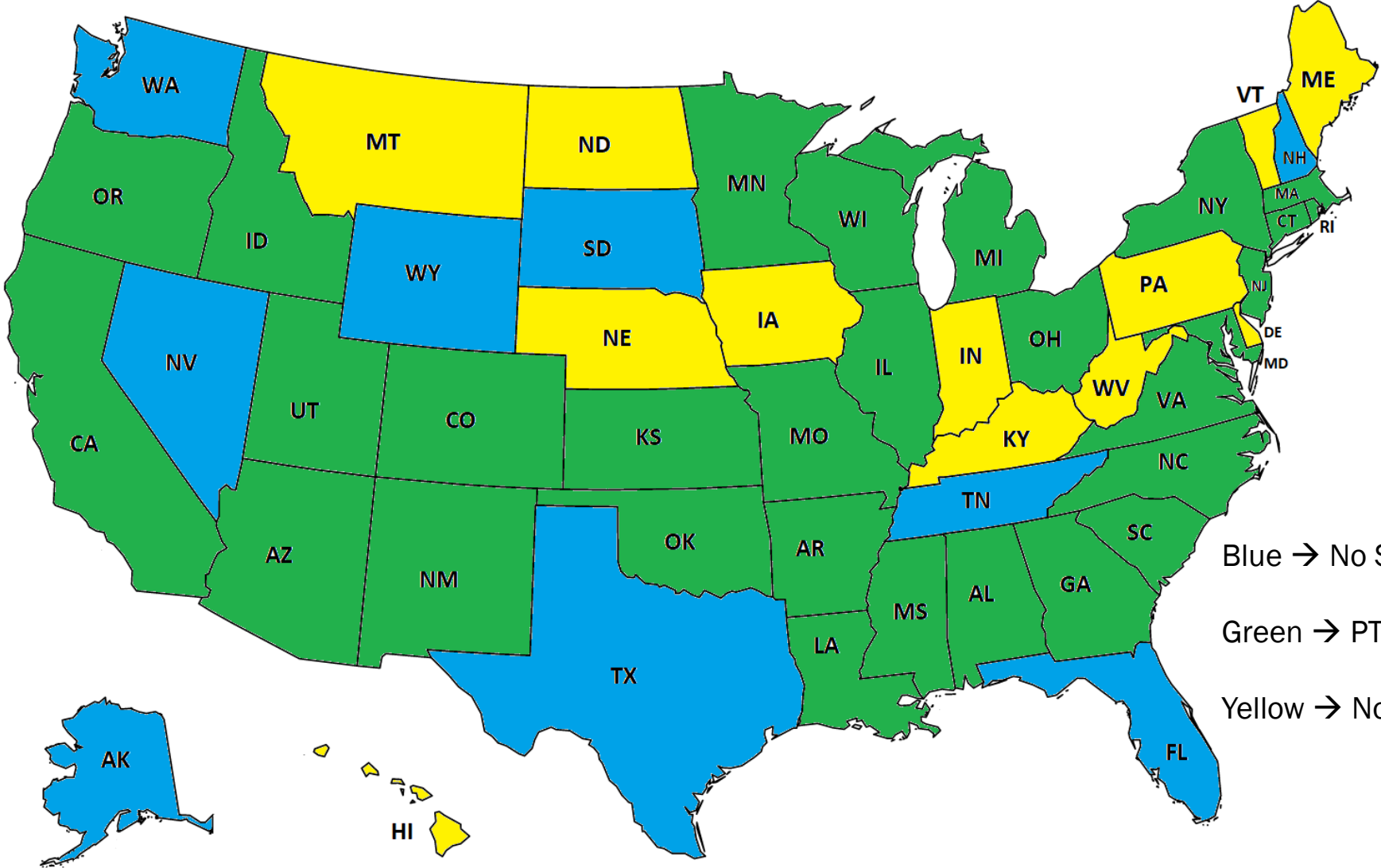
As a taxpayer's PTE income increases, their state tax liability increases, but they have a lower overall tax bill

How?

For each additional \$1 of PTE tax paid, the taxpayer:

- Gains at most \$.0875 of reduced state taxes (highest rate in VT 8.75%)
- Loses \$.10 because of the 90% credit (VT nets \$.0125)
- Gains likely between \$.24 and \$.37 of reduced federal taxes

Pass-Through Entity Tax/SALT Cap Workaround Map



Blue → No State Income Tax
Green → PTE Tax Enacted
Yellow → No PTE Tax

Pass-Through Entity Tax/SALT Cap Workaround (Continued)

- Administrative aids:
 - Elective
 - Only allowed for PTEs where all shareholders/members/partners are individuals, businesses can't qualify with C-Corp or other PTE owners.
 - All owners must elect the same treatment
- This structure also allows Vermont resident owners of out of state PTEs to take advantage of another state's PTE tax.

Earned Income Tax Credit

- Proposal: Increase Vermont's Earned Income Tax Credit (EITC) to 45% of the federal credit.
 - EITC helps put more money in the pockets of low- and modest-income Vermonters
 - DC, Maryland, New Jersey (arguably) have a more generous EITC than Vermont

Tax Year 2022 Eligibility for Federal Earned Income Tax Credit				
Children/Dependents Claimed	Maximum AGI (single, Head of Household)	Maximum AGI (married filing jointly)	Maximum VT Credit (Current 38%)	Maximum VT Credit (45% Proposed)
Zero	\$16,480	\$22,610	\$213	\$252
One	\$43,492	\$49,622	\$1,419	\$1,680
Two	\$49,399	\$55,529	\$2,342	\$2,774
Three	\$53,057	\$59,187	\$2,635	\$3,121

- Revenue Impact
 - \$5.25M base impact in FY24

Earned Income Tax Credit Continued

State	Maryland	District of Columbia	New Jersey	Vermont
State-level EITC as % of Federal EITC (TY 2022)	45%	70%	40%	38%
Is the credit refundable?	Yes	Yes	Yes	Yes
Differences in qualifications from federal	Age minimum requirement omitted; provides for ITIN filers	Same as federal for filers with qualifying children; without, income ceiling is \$37,455	Only available to filers with qualifying children	Same as federal

Social Security Exemption Expansion

- Proposal: Raise Vermont’s Social Security income (SSI) tax exemption threshold by \$15k
 - 39 states either fully exempt Social Security from income tax or don’t have income tax (including MA, NY, NH)
 - Last year Vermont raised the threshold by \$5,000 – but with Social Security COLA of 8.7%, more recipients will be pushed above the exemption threshold.

- Federal exemption flows through (excluded from AGI).

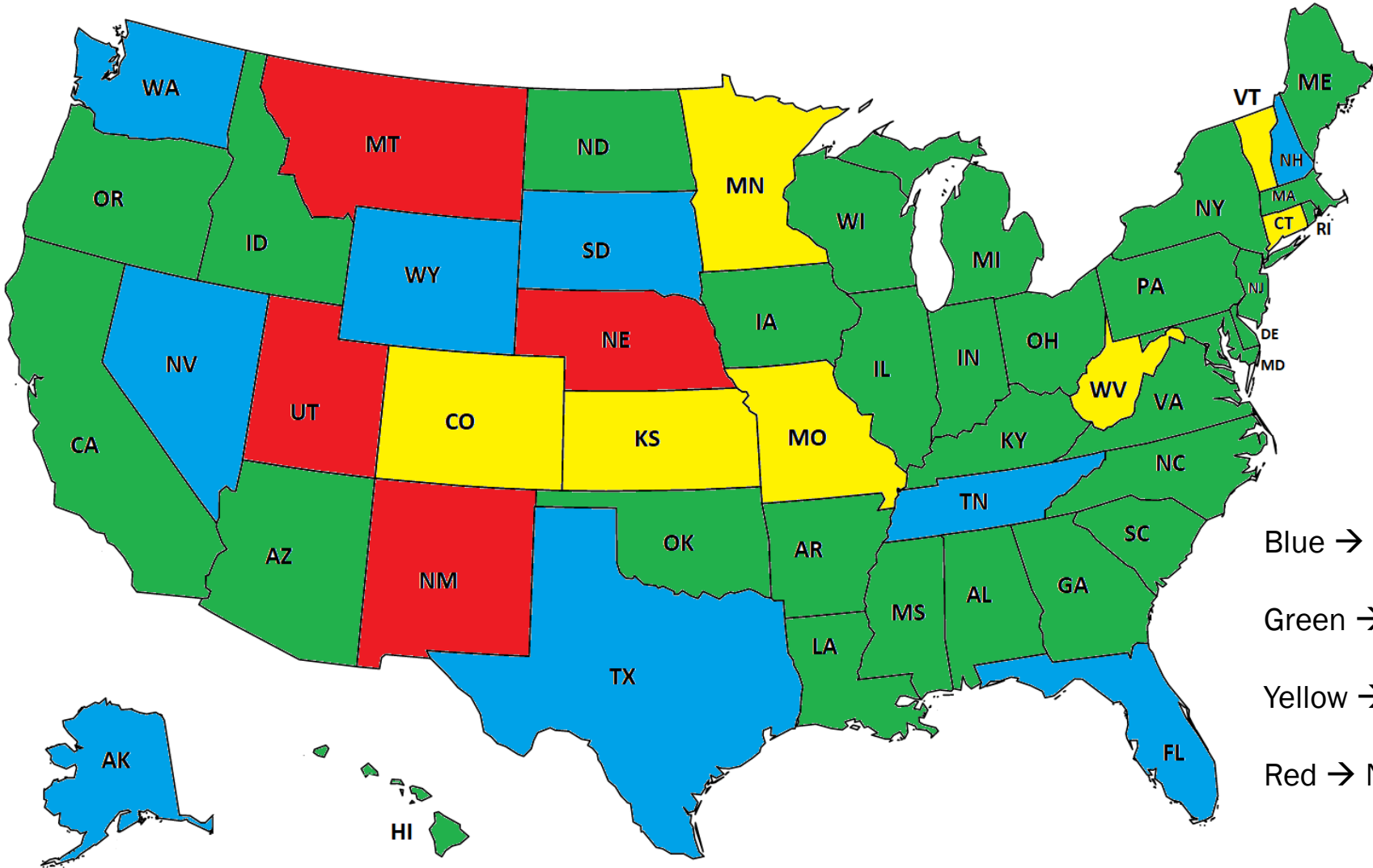
- For remaining taxable SSI:

	Current Law	Proposed Exemption
Fully exempt for	Single filers 0-50k Joint filers 0-65k	Single filers 0-65k Joint filers 0-80k
Partially exempt for	Single filers 50k-60k Joint filers 65k-75k	Single filers 65k-75k Joint filers 75k-85k

- Revenue Impact

- \$8.0M base impact in FY 24

Social Security Exemption Map

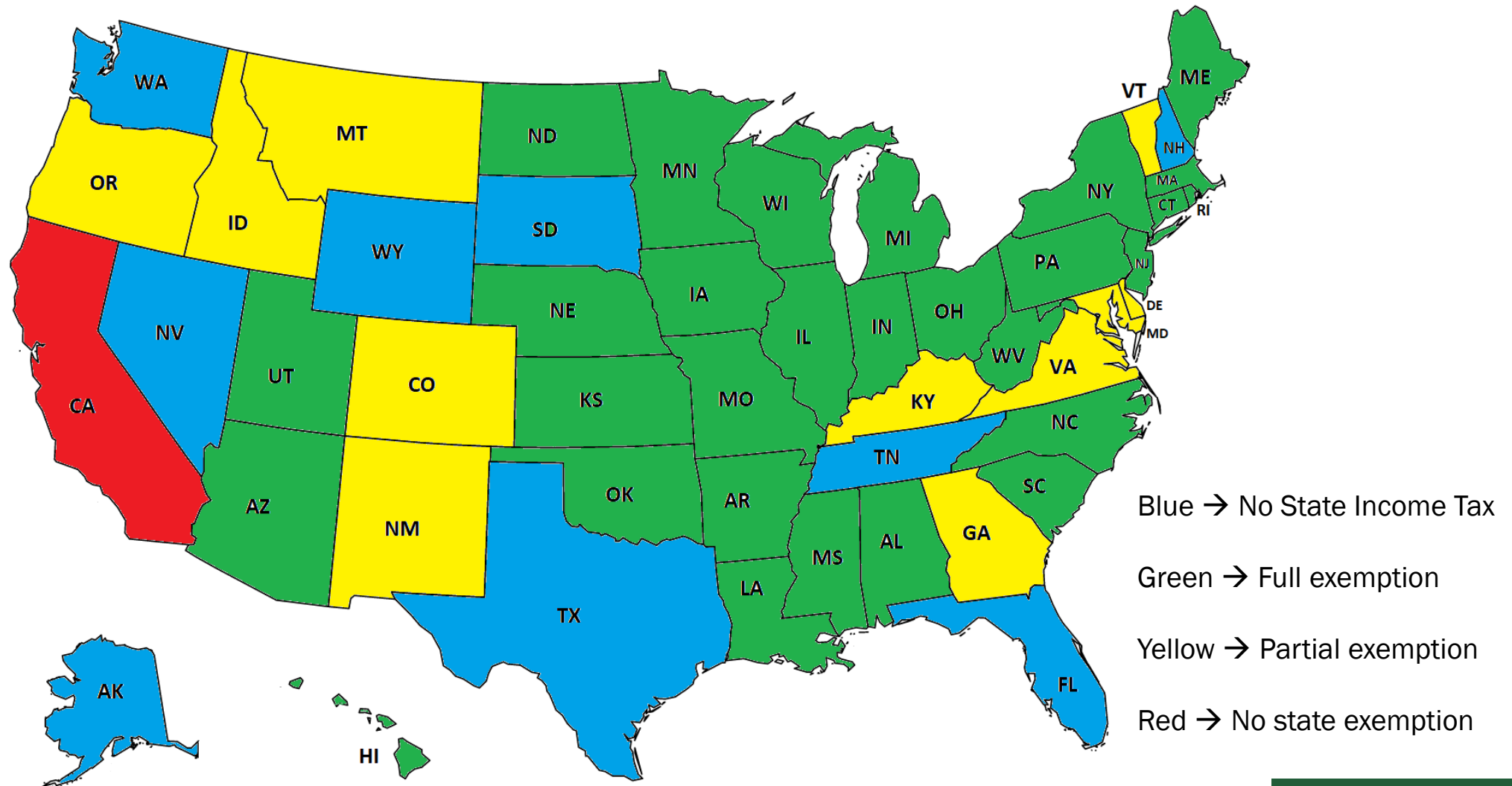


- Blue → No State Income Tax
- Green → Full exemption
- Yellow → Partial exemption
- Red → No state exemption

Military Pension & Survivor's Benefits Exemption

- Proposal: Exempt military retirement pay and survivor's benefits from Vermont personal income tax.
 - 38 states fully exempt military retirement pay or don't have state income tax
 - [JFO issue brief](#) notes that nationally 70% of military retirees are between ages 35 and 50.
- Current Vermont Law: Military retirees can deduct the first \$10,000 of a military pension if they meet the thresholds below AND they do not take a Social Security exemption
 - \$50k AGI single; \$65k MFJ
 - For partial: \$50-60k single; \$65-75k MFJ
- Revenue Impact
 - \$3.21 million base revenue reduction (\$2.9M military retirement pay + \$300k for survivors)

Military Pension & Survivor's Benefits Exemption Map



Alternative Minimum Tax

- Proposal: Repeal Vermont's Personal Alternative Minimum Tax
- Current Vermont law: 32 V.S.A. § 5822(6) → If AGI of taxpayer exceeds \$150,000, then the tax shall be a minimum of 3% of the taxpayers AGI.
- Relic of the pre 2018 reform where Vermont recognized itemized deductions.
- Total Revenue Impact: ~\$500,000

Alternative Minimum Tax (Continued)

- Who does it impact now?
- Taxpayers with high medical deductions
- Taxpayers following the law regarding Vermont's decoupling from bonus depreciation schedules
- Taxpayers with capital gain exclusions
- Taxpayers with high US bond income or railroad retirement income (illegal!)

Alternative Minimum Tax Data

AMT Triggers and Tax Impact – TY 2020			
Subtraction Type	Count	Tax Impact	Share of Impact
Bonus Depreciation	41	\$ (91,428)	20%
Capital Gains	65	\$ (40,231)	9%
Medical Expenses	116	\$ (311,417)	69%
Other	11	\$ (9,427)	2%
Grand Total	233	\$ (452,504)	

AMT Triggers and Tax Impact – TY 2021			
Subtraction Type	Count	Tax Impact	Share of Impact
Bonus Depreciation	32	\$ (95,116)	24%
Capital Gains	125	\$ (67,453)	17%
Medical Expenses	123	\$ (229,518)	57%
Other	20	\$ (7,714)	2%
Grand Total	300	\$ (399,800)	