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MEMORANDUM

To: House Committee on Ways and Means

From: Kirby Keeton, Office of Legislative Counsel

Date: December 19, 2025

Subject: Reconciliation Act of 2025; Tax and Finance Sections

Question Presented

You asked for a summary of the tax provisions of the 2025 federal budget reconciliation act, a description of any impacts on Vermont, and possible legislative responses to the parts affecting Vermont tax laws.

In the summary below, a change is effective for tax year 2025 unless stated otherwise.

Tax and Finance Sections of the Reconciliation Act of 2025

Section	Summary
Chapter 1. Income Tax for Families and Workers	
70101	Makes the federal individual marginal tax rates created by TCJA permanent. The rates are 10%, 12%, 22%, 24%, 32%, 35%, and 37%.
70102	Makes permanent the federal base standard deduction amounts set by TCJA. The amounts are $15,750 (single filers), $23,625 (head of the household), and $31,500 (joint filers). Amounts are adjusted annually for inflation.
70103	Makes permanent the TCJA elimination of the personal exemption tax deduction. Establishes a temporary personal exemption tax deduction of up to $6,000 for individuals aged 65 and older. The deduction phases out starting at $75,000 of AGI for individuals and $150,000 for joint filers. The new deduction is temporary for tax years 2025–2028.
70104	Increases the maximum federal child tax credit from $2,000 per qualifying to $2,200. Adjusts the maximum credit amount for inflation starting in tax year 2026. The following changes from TCJA are made permanent: the federal phaseout thresholds for the CTC of $200,000 (individuals) and $400,000

	(joint filers), the $500 nonrefundable child tax credit for dependents who are not qualifying children, and the refundable part (up to $1,400) of the child tax credit. Requires claimants to provide a work-eligible Social Security number. Current federal law already requires a qualifying child to meet identification requirements.
70105	The federal qualified business income tax deduction created by TCJA is made permanent and is expanded. Creates a minimum deduction of $400 for active qualified business income.
70106	Increases the federal base estate tax exemption from $5,000,000 to $15,000,000 starting in 2026. Updates the year in which inflation is to begin being calculated.
70107	Increases to the amounts for the federal alternative minimum tax exemption that was created by TCJA and makes them permanent. Starting in tax year 2026, reduces the threshold amounts of alternative minimum taxable income at which the exemption begins to phase out. The new amounts are $500,000 (individuals) and $1,000,000 (joint filers). Increases the phaseout percentage rate to 50 percent from 25 percent.
70108	The limit on the federal itemized deduction for home mortgage interest created by TCJA is made permanent. Starting in tax year 2026, allows certain mortgage insurance premiums to be included in the itemized tax deduction.
70109	The limit on the federal itemized deduction for unreimbursed personal casualty losses associated with a federally declared disaster, created by TCJA, is made permanent. Starting in tax year 2026, expands the deduction to losses caused by a state declared disaster.
70110	Elimination of the federal itemized deduction for miscellaneous expenses under TCJA is made permanent. The deduction for unreimbursed expenses for educators remains. Effective for tax year 2026.
70111	Replaces the Pease limitation on federal itemized deductions with a modified limitation.[1] Itemized deductions are now reduced by a fraction of 2/37 of the lesser of (1) the total amount of itemized deductions or (2) the amount of a taxpayer's taxable income that exceeds the top marginal rate.
70112	Makes bicycle commuting reimbursements federally taxable to employees by permanently excluding qualified bicycle commuting reimbursements from qualified transportation fringe and other commuting benefits. Effective tax year 2026.

[1] The Pease limitation reduced the benefit of itemized deductions for high-income taxpayers by reducing the value of a taxpayer's itemized deductions by 3% for every dollar of taxable income above the threshold. The phase-out of the value of itemized deductions was capped at 80% of the total value of itemized deductions.

70113	Retains the elimination of the federal deduction for moving expenses started by TCJA but starts allowing it for members of the intelligence community and Armed Forces in tax year 2026.
70114	Limits the federal deduction for wagering losses to 90 percent of losses and to the extent of wagering gains for the taxable year. Effective tax year 2026.
70115	Federal limitation on contributions to an ABLE account created by TCJA made permanent.
70116	Starting in tax year 2026, ABLE account contributions count as saver’s credit contributions. Starting in tax year 2027, qualified retirement contributions do not count toward the saver’s credit. The federal savers credit amount increased from $2,000 to $2,100.
70117	Federal allowance of rollovers from qualified tuition programs to an ABLE account made permanent.
70118	Permanently adds the Sinai Peninsula, Kenya, Mali, Burkina Faso, and Chad to list of qualified hazardous duty areas. Members of the military receive federal tax benefits when performing services in these areas.
70119	Exclusion from income of discharged student loans due to death or disability made permanent. Requires a Social Security number on tax return when a loan is discharged.
70120	Temporarily increases the limit on the federal SALT deduction cap to $40,000 (from $10,000). The cap inflates one percent per year. Applies to tax years between 2025–2028. Phases out the deduction for taxpayers with MAGI exceeding $500,000, with a minimum deduction of $10,000.
Chapter 2. Presidential Priorities	
70201	Creates a new deduction of up to $25,000 for qualified tip income. Available for occupations that customarily and regularly receive tips. The deduction is not an itemized deduction but is made from federal taxable income, which means it does not flow through to Vermont. Phaseout for taxpayers with MAGI exceeding $150,000 (individuals) and $300,000 (joint filers). Claiming the deduction requires a Social Security number and for married taxpayers to file jointly. The new deduction is temporary for tax years 2025–2028.
70202	Creates a new deduction of up to $12,500 (individuals) and $25,000 (joint filers) for qualified overtime compensation. The amount paid in excess of the regular rate can be deducted, up to the cap. The deduction is not an itemized deduction but is made from federal taxable income, which means it does not flow through to Vermont. Phaseout for taxpayers with MAGI exceeding $150,000 (individuals) and $300,000 (joint filers). Claiming the

	deduction requires a Social Security number and for married taxpayers to file jointly. The new deduction is temporary for tax years 2025–2028.
70203	Creates a new deduction of up to $10,000 for interest paid on a qualified passenger vehicle loan. Limited to vehicles with final assembly in the U.S. Phase out for taxpayers with MAGI exceeding $100,000 (individuals) and $200,000 (joint filers).[2] The deduction is not an itemized deduction but is made from federal taxable income, which means it does not flow through to Vermont. The new deduction is for interest paid or accrued in the taxable year on indebtedness incurred after 2024. The deduction is temporary for tax years 2025–2028.
70204	Creates a new individual retirement account for beneficiaries under 18 years of age (called "Trump accounts"). The account has an annual contribution limit of $5,000, which will be adjusted for inflation starting in 2027. Distributions are allowed after the beneficiary attains age 18 but there is a 10 percent penalty for distributions made before the beneficiary attains the age of 59.5. The penalty has some exceptions. Contributions do not reduce the gross income of a taxpayer making a contribution, but they are not included in the federal gross income of the account beneficiary. Employers may contribute up to $2,500 to an employee's account, or the account for an employee's dependent, and have the amount excluded from an employee's federal gross income. Authorizes the Treasury Secretary to deposit $1,000 into accounts for U.S. citizens born between 2025–2028.
Chapter 3. Businesses and Corporations	
70301	Permanently extends the 100 percent bonus depreciation allowed by TCJA.
70302	Allows a deduction for domestic research and experimental expenses in the year in which expenses are incurred. Previous law required capitalization and amortization over five or 10 years. A taxpayer may still elect to amortize these expenses over five years. Does not change treatment for foreign research and experimental expenses. Certain taxpayers can deduct these expenses retroactively.
70303	Allows a larger deduction of business interest expenses by allowing adjusted taxable income to be calculated without deductions for depreciation, amortization, or depletion. Allows a deduction for floor plan financing for certain trailers and campers.

[2] Restricted to new passenger vehicles assembled in the United States.

70304	Permanently extends the paid family medical leave (PFML) credit for qualifying employers created by TCJA. Allows the credit to be claimed for a percentage of premium amounts paid or incurred by an eligible employer for insurance policies that provide PFML. Expands the credit to be available in all states and reduces the minimum employee work requirement to not less than 20 hours per week. Changes are effective in tax year 2026.
70305	Makes permanent the exceptions from deduction limitations for food and beverages provided by an employer to employees in certain situations. Adds food and beverages provided on certain fishing vessels and fishing processing facilities to the exemption.
70306	Increases the maximum amount a taxpayer may expense the costs of a qualifying depreciable business asset in lieu of recovering the costs through depreciation. Increases the threshold for the maximum value of a property that can be expensed in this way. The maximum amount that can be expensed is increased from $1,000,000 to $2,500,000.
70307	Allows an additional first-year depreciation deduction equal to 100 percent of the adjusted basis of qualified production property. Allows a taxpayer to claim the deduction for certain nonresidential real property acquired after January 19, 2025, and before January 1, 2029.
70308	Increases the advanced manufacturing investment credit rate from 25 percent to 35 percent of a qualified investment in an advanced manufacturing facility for property placed into service after 2025.
70309	Provides spaceports the same treatment as airports under exempt facility bond rules, which limit whether a bond is federally guaranteed when a bonded facility is used by the U.S. government. Dictates that a bond for a spaceport shall not be treated as federally guaranteed merely because the U.S. government pays rent or a fee to use the spaceport.
70311	Modifies the rules for allocating and apportioning deductions to global intangible low-taxed income (GILTI) when determining a taxpayer’s foreign tax credit limitation. To determine the FTC limitation, a taxpayer must identify taxable income from foreign sources by allocating and apportioning deductions between U.S.-sourced gross income and foreign-sourced gross income. These deductions include interest expenses, stewardship expenses, and research and experimental expenses. The reconciliation act limits the deduction of U.S. shareholder allocable income for GILTI to the deductions under 26 U.S.C. §§ 250(a)(1)(B) and 164(a)(3) and any other deduction if it is allocable to GILTI. Any other deductions can only be allocated and apportioned to U.S.-sourced income.
70312	For GILTI, increases the credit allowable for foreign taxes imposed on controlled foreign corporations of the taxpayer. Specifically, it increases the allowance for deemed paid credit for taxes properly attributable to net controlled foreign corporation tested income (NCTI; previously called

	GILTI). Increased from 80 percent of a corporation's inclusion percentage to 90 percent.
70313	For purposes of the FTC limitation, if a U.S. entity maintains a place of business in a foreign country, the portion of taxable income from the sale or exchange outside the U.S. of property produced in the U.S. is treated as foreign-sourced taxable income if the property is attributable to the place of business in the foreign country. The treatment is limited to 50 percent of the total taxable income from the sale. Under previous law, the sale of property produced in the U.S. would be treated as U.S.-sourced income. Applies starting in tax year 2026.
70321	Decreases the Section 250 tax deduction allowed for foreign-derived intangible income from 37.5 percent to 33.34 percent and the deduction for GILTI from 50 percent of income included in gross income to 40 percent. Applies starting in tax year 2026. This section and the change made in section 70312 combine for an effective federal tax rate of 14 percent for both FDII and GILTI.[3]
70322	For FDII, changes how deduction eligible income (DEI) is determined by excluding certain income and gains from DEI. The following items will not be deduction eligible: • DEI does not include income or gain from the sale of property that provides rents or royalties. • DEI does not include any other property that is subject to depreciation, amortization, or depletion by the seller. • DEI is reduced by expenses and deductions, other than interest expense, and research or experimental expenditures, properly allocated to such income. These changes could lead to a greater FDII deduction for some taxpayers, although the deduction is limited by the Section 250(a)(2) taxable income limitation. Applies starting in tax year 2026.
70323	For FDII, eliminates reduction for deemed tangible income return. For GILTI, eliminates the reduction for net deemed tangible income return. Previously, there was a deemed reduction of 10 percent of qualified business asset investments.[4] This was the previous law approach to identifying intangible income by assuming a 10 percent return on tangible assets.

[3] U.S. Senate Committee on Finance, Section-by-Section Summary, at 16, available at: https://www.novoco.com/public-media/documents/senate-reconciliation-bill-section-by-section-06162025.pdf.

[4] These changes mean federal terminology in this area has also changed. FDII is now FDDEI and GILTI is now NCTI.

	This change decreases the incentive to lower tax paid on GILTI by investing in foreign assets, which were partially excluded from taxation. Applies starting in tax year 2026.
70331	Modifies the federal base erosion minimum tax (BEAT). BEAT was created when the U.S. changed from a worldwide system to a territorial system. Under TCJA, for tax year 2026, the rate on modified taxable income was supposed to increase from 10 percent to 12.5 percent. This section lowers the rate to 10.5 percent for tax year 2026 and beyond.
70341	For the business interest deduction, allows the Section 163(j) limitation to be calculated before interest capitalization. This creates an incentive for taxpayers to finance debt.
70342	Excludes Subpart F and GILTI/NCTI from adjusted taxable income for the business interest limitation. This disallows those types of income from increasing the total amount that can be deducted as business interest, resulting in more tax paid by taxpayers with large amounts of foreign income.
70351	Makes permanent the exclusion from foreign personal holding company income dividends, interest, rents, and royalties received by one controlled foreign corporation (CFC) from a related CFC to the extent attributable or properly allocable to income of the payor that is neither Subpart F income or income treated as effectively connected with conduct of a trade or business in the U.S. (called the CFC look-through rule).
S70352	Repeals the election for a specified foreign corporation to use a taxable year that is one month earlier than its majority U.S. shareholder’s tax year. Applies December 2025.
70353	Restores the limitation on downward attribution of stock ownership (when a shareholder, partner, or beneficiary of an entity owns 50 percent or more of the entity, the entity is treated as owning the stock owned by that person). This restores Section 958(b)(4), which dictates that stock owned by a foreign person is not attributed downward to a U.S. person. This means that a wholly owned domestic subsidiary of a foreign corporation is not treated as owning stock in other foreign corporations owned by the foreign parent. This can affect whether a foreign corporation is considered a CFC.
70354	Provides that if a foreign corporation is a CFC at any time during a taxable year, each U.S. shareholder that owns stock in the corporation must include in gross income their pro rata share of the corporation’s Subpart F income for the CFC’s tax year. Similar provisions also apply to GILTI/NCTI income.
Chapter 4. Families, Communities, and Small Business	
70401	Permanently increases the maximum federal employer-provided child care credit from $150,000 to $500,000 and creates a separate maximum credit amount for small businesses of $600,000. The credit caps are now adjusted

	for inflation. The percentage of covered expenses increases from 25 percent to 50 percent for small businesses and 40 percent for other businesses. The credit now allows small businesses to pool resources and for businesses to use a third-party intermediary to facilitate child care services.
70402	Makes up to $5,000 of the federal adoption credit refundable. Adjusted for inflation. Current law allows a carryforward for the remainder.
70403	For the federal adoption credit, allows Indian tribal governments the same ability as state governments to determine whether a child has “special needs.”
70404	Increases the maximum federal exclusion for dependent care assistance from $5,000 to $7,500. This exclusion allows employees to set aside pre-tax funds to cover qualified expenses. Applies to tax year 2026.
70405	Expands the phaseout for the federal child and dependent care credit. The maximum credit rate is increased to 50 percent (from 35 percent) for AGIs of $43,000 or less. The 50 percent rate begins to phase down at $15,000 of AGI. For AGIs between $43,001 and $75,000 for an individual return, and $86,001 and $150,000 for a joint return, the credit rate is 35 percent. The credit rate is phased down to 20 percent between $75,001 and $105,000 for an individual return and between $150,001 and $210,000 for a joint return.
70411	Creates a new federal credit for contributions made to certain scholarship granting organizations for elementary and secondary school expenses. The credit amount is up to $1,700 and is reduced by the amount of any allowed state credit. States must voluntarily elect to participate in the program. Scholarship amounts are excluded from gross income of the taxpayer, or a dependent, receiving a scholarship. Applies starting in tax year 2027.
70412	Makes permanent the exclusion from gross income and employments taxes of up to $5,250 of student loan payments by an employer for an employee.
70413	Expands the types of educational expenses that can be paid using distributions from a federal 529 plan to include several expenses relating to elementary and secondary school.
70414	Allows federal 529 plan contributions to be used for qualified postsecondary credentialing expenses.
70415	Creates tax rate brackets for the federal excise tax on net investment income paid by certain private colleges and universities. Institutions with a student-adjusted endowment of $750,000 or more will pay a higher rate. The current excise tax rate is 1.4 percent of net investment income and this change increases the rate up to eight percent for institutions with a student-adjusted endowment of $2,000,000 or more. Exempts qualified religious institutions from paying the excise tax.

70416	Expands the application of tax on excess compensation paid by tax-exempt organizations so that it applies to any employee receiving remuneration in excess of $1,000,000. The tax is equal to the corporate tax rate multiplied by any remuneration exceeding $1,000,000 paid to a covered employee.
70421	Permanently renews and modifies the opportunity zones system created by TCJA. Starting in 2027, OZ designations will be implemented on a 10-year rolling basis. Changes some definitions relating to OZs.
70422	For the federal low-income housing tax credit, permanently increases the state allocation ceiling by 12 percent and lowers the bond-financing threshold to 25 percent for projects financed by bonds. The state allocation ceiling was previously increased by 12.5 percent between 2018 and 2021. Applies starting in 2026.
70423	Permanently extends the federal New Markets Tax Credit, which is available for private capital investments in eligible low-income communities.
70424	Creates a permanent federal charitable contributions deduction for taxpayers who do not itemize. The deduction is up $1,000 for single filers and up to $2,000 for joint filers. Limited to certain cash contributions. Applies starting in tax year 2026.
70425	Reduces the amount of an individual's charitable contributions that can be deducted by 0.5 percent of the taxpayer's contribution base. Permanently extends the increased contribution limit for cash gifts made to qualifying charities.
70426	The charitable deduction for corporations requires a minimum of one percent of a corporation's taxable income to be charitable contributions. In other words, the first one percent of taxable income worth of charitable contributions cannot be deducted.
70427	Permanently increases the "cover over" for distilled spirits (rum) imported from Puerto Rico and the U.S. Virgin Islands. This results in an increase of federal alcohol excise tax revenue that is transferred to those territories when the tax is paid on those imports.
70428	Exempts certain investment and development activities relating to fisheries in the Bering Sea and Aleutian Islands from federal income taxation.
70429	Increases the amount of expenses relating to certain subsistence whaling activities that can be treated as a charitable deduction from $10,000 to $50,000.
70430	Allows certain residential construction contracts to use uniform capitalization rules for accounting rather than the percentage of completion method.
70431	Expands the federal exclusion for gains from qualified small business stock to allow a 50 percent exclusion for QSBS held for three years, 75 percent

	exclusion for QSBS held for four years, and 100 percent exclusion for QSBS held for five years. Increases the per-issuer exclusion cap for QSBS from $10,000,000 to $15,000,000. The corporate-level aggregate-asset ceiling is increased to $75,000,000.
70432	Modifies requirements for third-party settlement organizations to eliminate reporting requirements with respect to transactions of payees unless they have earned more than $20,000 on more than 200 separate transactions in a tax period. This will reduce the number of 1099-Ks issued and reverses provisions from ARPA that would have caused third-party settlement organizations to issue more 1099-Ks.
70433	Increases the reporting threshold for payments by a business for services performed by an independent contractor or subcontractor to $2,000 (from $600) and adjusts it for inflation.
70434	Provides qualified sound recording productions tax treatment similar to qualified film, television, and live theatrical productions by applying special expensing rules.
70435	Permanently allows certain financial and insurance institutions to exclude from gross income 25 percent of the interest income derived from qualified real estate loans for properties used for agriculture, fishing, seafood, and aquaculture.
70436	Eliminates federal transfer tax on certain firearms other than machine guns and destructive devices. Silencers, short-barreled rifles, and short-barreled shotguns are no longer subject to the tax.
70437	Allows the portion of tax due for capital gains from the sale of qualified farmland property to a qualified farmer to be paid in four installments across four successive tax years.
70438	Extends the rules for treatment of certain disaster-related personal casualty losses created by the Taxpayer Certainty and Disaster Tax Relief Act of 2020.
70439	Amends the subsidiary asset test required to qualify for tax treatment as a real estate investment trust (REIT). Currently, a REIT cannot have more than 20 percent of the value of its total assets represented by securities of one or more taxable REIT subsidiaries. Starting in tax year 2026, the 20 percent threshold is changed to 25 percent.
Chapter 5. Energy and Environment	
70501	Terminates the federal tax credit for previously owned clean vehicles. Effective 90 days after July 4, 2025.
70502	Terminates the federal tax credit for new clean vehicles. Effective 180 days after July 4, 2025.

70503	Terminates the federal tax credit for qualified commercial clean vehicles. Effective 180 days after July 4, 2025, and places limitations on how the credit can be used before it terminates.
70504	Terminates the federal alternative fuel vehicle refueling property credit. Applies to property placed in service after July 3, 2026.
70505	Terminates the federal energy efficient home improvement credit. Effective 180 days after July 4, 2025.
70506	Terminates the federal residential clean energy credit. Effective 180 days after July 4, 2025.
70507	Terminates the federal energy efficient commercial building deduction. Applies to property constructed after July 3, 2026.
70508	Terminates the federal new energy efficient home credit. Applies to homes acquired after July 3, 2026.
70509	Terminates the federal cost recovery for qualified clean energy facilities, property, and technology. Previously, taxpayers could recover costs over five years for certain clean energy properties instead of typical depreciation or amortization. Effective July 4, 2025.
70510	Limits the zero-emission nuclear power production credit by disallowing the credit if the taxpayer uses fuel produced in certain places or by certain entities and also prohibits the credit for certain foreign entities. Applies starting with tax year 2028.
70511	Terminates the clean hydrogen production credit for facilities that begin construction after 2025.
70512	Phases out the federal clean electricity production credit for wind and solar technology by reducing the credit amount for calendar years 2026 and 2027 and ending the credit in 2028. The phaseout for hydropower, nuclear, and geothermal begins in 2033 and the credit ends in 2036. Prevents the credit for wind and solar leasing to residential customers. Prevents the credit for facilities connected with prohibited foreign entities.
70513	Phases out the federal clean electricity investment credit similarly to the phaseout for clean electricity production credit.
70514	Phases out the federal advanced manufacturing production credit. The phaseout begins in 2031 and the credit is terminated in 2034. Places restrictions on the credit relating to prohibited foreign entities.
70515	Prevents funds for the advanced energy project credit program from being reissued when a taxpayer has failed to certify the project and the credit has been reclaimed by the U.S. government. Previously, the credits would be reissued to a different taxpayer for a different project.
70521	Extends the clean fuel production credit through tax year 2031 and reduced the credit amount for fuel produced from feedstocks produced or grown

	outside the U.S. Places other restrictions on the credit and prevents use of the credit by prohibited foreign entities.
70522	Restricts access to the federal credit for carbon oxide sequestration for prohibited foreign entities.
70523	Allows intangible drilling and development costs to be included when determining corporate alternative minimum tax liability. This will decrease federal taxes owed by some corporations with intangible oil and gas drilling costs.
70524	Adds income from hydrogen storage, carbon capture, advanced nuclear, hydropower, and geothermal energy to "qualifying income" of certain publicly traded partnerships treated as corporations. A PTP must have 90 percent of gross income from qualifying sources to be treated as partnerships for tax purposes.
70525	Allows a refund of federal fuel excise taxes paid on fuel indelibly dyed for off-road purposes. Effective 180 days after July 4, 2025.
70531	Eliminates the de minimis exemption for duties and fees owned on certain imports valued up to $800. Creates civil penalties for a violation. Effective July 1, 2027.
Chapter 6. Deductions, Tax Credits, and Other Reforms	
70601	Makes permanent the TCJA limitation on excess business losses for noncorporate taxpayers. This disallows a deduction for those taxpayers for the amount that aggregate business deductions exceed aggregate business income, plus a threshold of $250,000 (for individual returns). Starting in tax year 2025, excess business losses from previous years are used to determine excess business losses in subsequent years.
70602	Clarifies ambiguous language in the federal statute on the tax treatment of payments from a partnership to a partner. Clarifies that the statute is to be followed unless provided otherwise.
70603	Expands the federal deduction limitations relating to excess employee compensation. Provides that a publicly held corporation must determine certain highly compensated employees on a controlled group basis, which expands the pool of individuals who could be counted and be subject to the deduction limitation.
70604	Imposes a 3.5 percent excise tax on certain remittance transfers to be paid for by the sender. These are noncommercial transfers of money from people working in the U.S. to people abroad. Includes an exception for certain transfers and a refundable tax credit for excise tax paid by people with a work-eligible SSN.
70605	Adds enforcement provisions relating to eligibility for the employee retention tax credit and employment tax refund claims.

70606	Adds Social Security number requirements to claiming the federal American Opportunity Tax Credit and Lifetime Learning Tax Credit. Applies starting in tax year 2026.
70607	Appropriates $15,000,000 for a report on replacing any direct e-file programs run by the IRS with a public-private alternative and other related topics.

Notable Changes That Do Not Flow Through to Vermont

Personal Exemption for Taxpayers Aged 65 and Older (Sec. 70103). The new personal exemption is a below-the-line deduction that can be taken with the standard deduction or with itemized deductions. This will not flow through to Vermont.

Vermont Child Tax Credit (Sec. 70104). Subsection 5830f(a) of Title 32 already disregards the taxpayer identification number requirements under 26 U.S.C. § 24(e) and (h)(7).

Estate and Gift Taxes (Sec. 70106). The increase in the base federal exemption desynchronizes Vermont from the federal estate and gift taxes. Vermont is already decoupled from the U.S. tax code for purposes of the exemption, but this change will likely cause taxpayers to be required to file a pro forma federal return for taxable estates between $5,000,000 and $14,999,999.

SALT Deduction Cap (Sec. 70120). This affects some Vermont taxpayers when paying federal taxes but does not affect the State.

Taxation of Tip Income (Sec. 70201). The deduction for qualified tip income will not flow through to Vermont because it is not included in AGI.

Taxation of Qualified Overtime Compensation (Sec. 70202). The deduction for qualified overtime income will not flow through to Vermont because it is not included in AGI.

Interest on Passenger Vehicle Loans (Sec. 70203). The deduction for auto loan interest will not flow through to Vermont because it is not included in AGI.

Bonus Depreciation on Certain Business Property (Sec. 70301). Vermont already disregards federal bonus depreciation (26 U.S.C. § 168(k)) when calculating taxable income and net income. However, the new special depreciation allowance for qualified production property is located at 26 U.S.C. § 168(n), meaning that Vermont is not decoupled from that change. See below regarding section 70307 for more information.

Federal Credit for Contributions to Scholarship Granting Organizations (Sec. 70411). This would not directly flow through to the State because it is a federal tax credit. Contributions to Vermont organizations would only be eligible for the credit if Vermont chooses to participate in the federal program by having the Governor submit a list of qualifying organizations to the Treasury Secretary.

Expansion of Expenses Allowable for 529 Plan Distributions Secs. 70413 and 70414). Vermont's credit for Vermont Higher Education Investment Plan is decoupled from U.S. law for purposes of how distributions can be used. Vermont does not allow distributions to be used for any elementary or secondary education expenses.[5]

Charitable Contribution Deduction for Non-Itemizers (Sec. 70424). The deduction does not flow through to Vermont because it is not included in AGI.

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[5] However, a taxpayer's use of these distributions can be difficult to track and audit. It is therefore possible that a taxpayer could use VHEIP distributions for a purpose allowed federally, but not allowed in Vermont, and nonetheless avoid paying Vermont's penalty.

Changes That Flow Through to Vermont

Social Security Number Requirements (Sec. 70119). The new identification requirement for the exclusion of discharged student loans due to death or disability would affect Vermont returns in cases where a taxpayer was unable to provide a Social Security number and was required to pay tax on the discharged loan amount.

Trump Accounts (Sec. 70204). Employer contributions to an account that are excluded from federal gross income would flow through to Vermont unless the definition of taxable income is amended to include an add-back.

Domestic Research and Experimental Procedures (Sec. 70302). The change in treatment of the deduction for domestic research and experimental expenses would flow through to Vermont.[6] The changes in how expenses can be calculated could cause a short-term reduction in revenue unless Vermont decouples from how these expenses are deducted.

Amended Limitation on Business Interest Deduction (Secs. 70303 and 70341). These sections change the business interest deduction so that the deduction is limited to a taxpayer's business interest income, floor plan financing interest, and 30 percent of the taxpayer's adjusted taxable income (ATI). The calculation for ATI was changed so that depreciation and amortization can be included in ATI, allowing for a greater deduction.

This deduction is for the interest on indebtedness and the changes provide a tax benefit to corporations that take on more indebtedness.[7]

These changes flow through to Vermont because the deductions reduce the taxable income of the taxpayer under the laws of the United States and the definition of "Vermont net income" for corporate taxpayers does not alter how the business interest deduction is calculated or have an add-back for any part of it.

Exceptions from Business Meals Deduction (Sec. 70305). The exceptions from deduction limitations for food and beverages provided by an employer to employees in certain situations will flow through to Vermont with limited impact.

Increased Limitation on Expensing of Depreciable Business Assets (Sec. 70306). The increase in the maximum amount a taxpayer may expense for the costs of a qualifying depreciable business asset flows through to Vermont.

Special Depreciation Allowance for Qualified Production Property (Sec. 70307). Vermont is not decoupled from 26 U.S.C. § 168(n), which means the new depreciation allowance for qualified production property will flow through. Sunsets after 2028.

Foreign-Derived Intangible Income and Global Intangible Low-Taxed Income (Secs. 70312, 70321, 70322, and 70323). Starting in tax year 2026, these sections create an

[6] Vermont allows a credit equal to 27 percent of the federal research and development credit. 32 V.S.A. § 5930ii. It is unclear whether this change will cause taxpayers to claim less federal credit, and thereby reduce the revenue cost of the Vermont credit. The Vermont credit may not be affected because most taxpayers may claim the full federal credit and use the basis adjustment for domestic research and experimental expenditures.

[7] Note that the change to the definition of adjusted taxable income for the business interest limitation and the change involving interest capitalization will slightly increase Vermont revenue even though the total impact of changes to the limitation on business interest decreases revenue.

effective federal tax rate for both FDII and GILTI of about 14 percent. This is higher than the previous rate of about 10.5 percent. The U.S. domestic corporate rate is 21 percent. For comparison, the agreed upon global rate under the OECD's Pillar Two is 15 percent. The change relating to QBAI deduction flows through to Vermont but the changes to the foreign tax credit do not. The QBAI changes result in an increase in taxes paid, therefore, there is expected to be a revenue increase for Vermont.

Changes in Terminology Relating to the Taxation of Foreign-Derived Income. FDII is now changed to foreign-derived deduction eligible income (FDDEI) to reflect changes to federal definitions and rules, including the elimination of the deemed tangible income return. GILTI is changed to Net CFC Tested Income (NCTI) to reflect the removal of the net deemed tangible income return.

A taxpayer's FDII deduction is now FDDEI multiplied by the FDII rate. NCTI no longer excludes a portion of QBAI and now only excludes tested losses.

Restoration of the Limitation on Downward Attribution of Stock Ownership (Sec. 70353). This will flow through to Vermont with limited impact.

Changes to Pro Rata Share Rules (Sec. 70354). The changes affecting how U.S. shareholders of controlled foreign corporations must report gross income will flow through to Vermont and increase revenue.

Dependent Care Assistance (Sec. 70404). The increase in the exclusion limit for DCA flows through to Vermont because it is excluded from AGI.

Child and Dependent Care Credit (Sec. 70405). The expanded phaseout of the federal credit will flow through to Vermont. Vermont allows a credit equal to 72 percent of the federal credit.

Exclusion for Employer Payment of Student Loans (Sec. 70412). The exclusion from gross income flows through to Vermont. The temporary allowance of this exclusion already affected Vermont, but this change makes it permanent.

Opportunity Zones Extension (Sec. 70421). The permanent renewal of opportunity zones flows through to Vermont and will have an impact after 2027. These zones exist now but may be expanded and have a greater revenue impact later.

Low-Income Housing Credit (Sec. 70422). The "small state minimum" received by Vermont for the allocated credit will increase by 12 percent, which may increase the number of affordable rental housing projects supported per year. The lower bond-financing threshold may also incentivize some developers to start projects because the amount that must be borrowed through VHFA is decreased to 25 percent.

Charitable Deduction for Corporations (Sec. 70426). The one percent floor on a corporation's charitable contributions will flow through and slightly increase revenue. This flows through because Vermont net income for corporate taxpayers is not decoupled from the charitable deduction available for federal corporate income tax.

Accounting Changes for Certain Residential Construction (Sec. 70430). The change allowing certain residential construction contracts to use uniform capitalization rules for accounting rather than the percentage of completion method will flow through to Vermont. The impact should be extremely limited.

Expanded Exclusion of Gains from Qualified Small Business Stock (Sec. 70431). Vermont has not decoupled from federal law relating to the treatment of gains from qualified small business stock. The expanded exclusion and increased exclusion cap flow through to Vermont.

Exclusion of Interest on Loans Secured by Certain Agricultural Property (Sec. 70435). Vermont exempts taxpayers from corporate income tax if they are subject to the franchise tax on financial institutions. The exclusion applies to banks insured by the FDIA, domestic entities owned by a bank holding company, insurance companies, domestic entities owned by an insurance company, and the Federal Agricultural Mortgage Corporation. This new exclusion may not flow through to Vermont for many taxpayers because these taxpayers do not pay corporate income tax in Vermont. Accordingly, the expected revenue impact is minor.

Capital Gains from Sale of Farmland Paid in Four Installments (Sec. 70437). It is currently unclear how the option for some taxpayers to pay capital gains in four installments at the federal level will affect Vermont tax returns. The impact may become clear when the IRS publishes new returns. Assuming it may cause taxpayers to also pay Vermont in four installments, it’s possible that it would cause some taxpayers to become subject to Vermont’s alternative minimum tax. It may also cause administrative issues when taxpayers leave the state before all installments are paid.

Deduction Limitations to Excess Employee Compensation (Sec. 70603). The amended deduction limitations will flow through to Vermont but due to the nature of corporate filings, the impact may not be detectable.