

# Proposed Vermont Response to HR1

House Committee on Ways and Means

Patrick Titterton, Senior Fiscal Analyst

February 25, 2026



# H.R.1 Changes to Business and Corporate Income Taxes



# H.R.1 Changes to Business and Corporate Taxes

- There were many changes made to business and corporate income taxes that are considered “above the line” and will flow through to Vermont.
  - The deduction for domestic research and development expenses,
  - limitation on business interest deduction,
  - limitation on expensing for depreciable business assets,
  - special depreciation allowance for qualified production property,
  - foreign derived intangible income and global intangible low-taxed income,
  - changes to pro rata share rules,
  - charitable deduction for corporations,
  - expanded exclusion of gains from qualified small business stock, and
  - other miscellaneous business and corporate provisions.
- HR1 also expanded the Child and Dependent Care Credit, which is PIT but flows through.



# Updated HR1 Vermont Revenue Impact Estimates

- The estimates shared in January were based on preliminary analysis with limited information.
- JFO and the Tax Department have been working together to update these estimates.
- This update is based on:
  1. Additional information including federal updates on receipts
  2. Monitoring what other states have been experiencing and how HR1 is affecting their revenues
  3. Updated methodology for calculating some provisions



# Updated HR1 Vermont Revenue Impact Estimates

<u>H.R.1 provisions that will flow through to VT with normal conformity</u>	<u>IRC Section</u>	<u>FY26 (Millions)</u>	<u>FY27 (Millions)</u>
Child and Dependent Care Tax Credit Expansion	21	0.0	-1.0
Full Expensing of Domestic R&E	174(a)	-18.9	-19.9
Amended Limitation on Business Interest Deduction	163(j)	-3.1	-3.7
More Generous Expensing of Depreciable Assets	179	-0.9	-1.9
Special Depreciation for Qualified Production Property	168(n)	-0.8	-11.7
International Tax Provisions	250(a), 951A	2.4	2.8
Pro-Rata Share Rules	951, 951A	0.0	0.3
Charitable Deductions for Corporations	170(b)(2)(A), (d)(2)	0.0	0.5
Expanded Exclusion of Qualified Small Business Stock	Sec. 1202(a)(1)	0.0	0.0
Miscellaneous Business and Corporate Provisions		0.7	0.8
<b>Total</b>		<b>-21.3</b>	<b>-34.3</b>



# The Deduction for Domestic Research and Experimental Expenses

- H.R.1 changes how corporations calculate their R&E expenses deduction amount.
- Starting in 2022 (TCJA), these expenses were required to be amortized over five years, which meant the benefit from the deduction was realized incrementally over that period.
- Prior to TCJA, incurred R&E expenses could be deducted immediately. The H.R.1 changes revert back to pre-TCJA treatment.
- H.R.1 also makes this change retroactively to include any R&E expenses that have not been already deducted since 2022.
- This will likely front-load the cost of the deduction for R&E expenses.
- Because Vermont is coupled to this provision, linking up would cause it to flow through to the State.



# Amended Limitation on Business Interest Deduction

- H.R.1 expanded the limit to which corporations can deduct interest paid on loans for a business purpose.
- The limit on business interest deductions is limited by the sum of its business interest *income*, floor plan financing interest, or 30% of their adjusted taxable income.
- H.R.1 expanded the amount of business interest paid that can be deducted from 30% to 50%.
- Because Vermont is coupled to this provision, linking up would cause it to flow through to the State.



# Limitation on Expensing For Depreciable Business Assets

- H.R.1 increases the maximum amount that a taxpayer may expense for the cost of a qualifying depreciable business asset in lieu of recovering the costs through depreciation.
- The maximum amount that can be expensed increased from \$1 million to \$2.5 million and will be indexed for inflation annually.
- Because Vermont is coupled to this provision, linking up would cause it to flow through to the State.



# Special Depreciation Allowance for Qualified Production Property

- H.R.1 now allows a deduction for qualified production property of 100% of its adjusted cost basis.
- This 100% bonus depreciation can be used for qualified nonresidential property used in manufacturing or production of tangible personal products. Further, this is largely limited to agricultural and chemical production.
- These properties are typically depreciated over 39 years, but this change would allow that amount to be fully claimed up front.
- This change applies to properties built or bought after January 19, 2025 and before January 1, 2029.
- Vermont will need to decide whether to couple or decouple from this new provision.



# Foreign Derived Intangible Income and Global Intangible Low-Taxed Income

- H.R.1 increased the base used to calculate foreign derived intangible income (FDII) while also increasing the percentage of this income that can be deducted, effectively lowering the effective tax rate.
- The bill also eliminated a deduction of 10% of the tax basis of qualified tangible assets in other countries (QBAI) used to calculate global intangible low-taxed income (GILTI), which increases the base amount of this income.
- FDII was renamed foreign-derived deduction eligible income and GILTI was renamed net controlled foreign corporation tested income.
- Vermont is coupled to the federal treatment of this kind of income so linking up would cause it to flow through to the State.



# Changes to Pro Rata Share Rules

- H.R.1 changes the treatment of controlled foreign corporation (CFC)
  - A foreign corporation is a CFC if at least 50% of voting power or value of the stock are held by U.S. shareholders.
- Each U.S. shareholder must include in their gross income their pro rata share of the CFC's passive income in that tax year.
- Taxpayers that hold stock in CFC's will have to report more gross income than they would have previously.
- Because Vermont is coupled to this provision, linking up would cause it to flow through to the State.



# Charitable Deductions for Corporations

- Previously, corporations could deduct charitable contributions equal to up to 10% of their taxable income.
- H.R.1 makes a change so that only contributions made in excess of 1% and up to 10% of taxable income can be deducted.
- This change reduces the amount that can be claimed by 1%, thus reducing the maximum deductible amount.
- Because Vermont is coupled to this provision, linking up would cause it to flow through to the State.



# Expanded Exclusion on Gains from Qualified Small Business Stock

- H.R.1 allows stock for corporation issued after July 5, 2025 with aggregate gross assets (AGA) below \$75 million to qualify as a Qualified Small Business Stock (QSBS).
  - This is an increase from the previous \$50 million in AGA and will allow more businesses to qualify to issue QSBS.
- Investors who buy these shares can exclude 50% of capital gains if held for 3 years, 75% if held for 4 years, and 100% if held for 5 years.
- H.R.1 also increase the per-issuer exclusion cap from \$10 million to \$15 million.
- Because Vermont is coupled to this provision, linking up would cause it to flow through to the State.



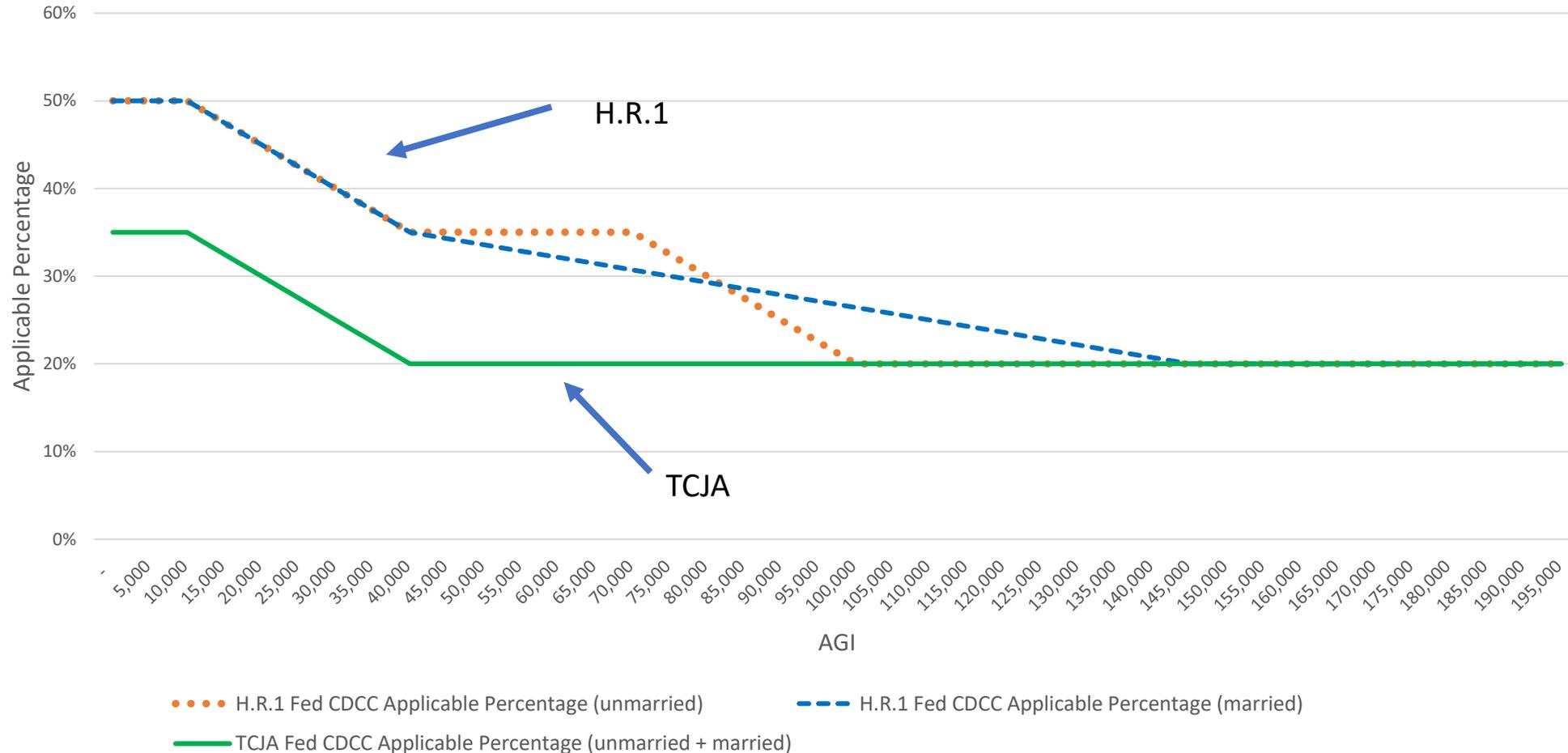
# Federal changes to Child and Dependent Care Credit (CDCC)

- H.R.1 expanded the phase out for the federal CDCC and increased the maximum credit rate to 50% from 35%.
  - Meaning qualifying expenses can be claimed for the credit at a rate of 50 cents per dollar.
- Vermont has a State CDCC that is refundable and set equal to 72% of what the claimant receives on their federal return.
  - Vermont does this for certain other State level credits like the Earned Income Tax Credit.
- Typically, because federal credits are calculated “below the line” they do not flow through to Vermont unless there is a State level credit linked directly to the federal calculation.
- The 2025 Tax Expenditure Report projected the CDCC to result in \$4.8 million in forgone revenue in FY 2026 under previous law.



# Federal changes to CDCC

Change in Percent of Eligible Expenses Claimed for Fed CDCC



# Proposed Language



# The Proposed Language Would...

- Link Vermont up to:

- Child and Dependent Care Tax Credit Expansion
- Amended Limitation on Business Interest Deduction
- More generous Expensing of Depreciable Assets
- Pro Rata Share Rules
- Charitable Deductions for Corporations
- Other Miscellaneous Business and Corporate Provisions

- Decouple Vermont from:

- Deduction of Research and Experimental Expenses
- Special Depreciation for Qualified Production Property
- Qualified Small Business Stock Exclusion
- Section 250 Deduction (NCTI and FDDEI)

- Additionally:

- Increase the annual cap on Downtown and Village Center Tax Credits than can be awarded annually by \$2 million (\$5 million total)
- Increase the State Research and Development Credit from 27% to 75% of the federal credit allowed for R&D expenditures within Vermont.



# Net Estimated Changes to State Revenue

<b>Proposed Language</b>	<b>IRC Section</b>	<b>FY26 (Millions)</b>	<b>FY27 (Millions)</b>
Link up to Child and Dependent Care Tax Credit Expansion	21	0.0	-1.0
Link up to Amended Limitation on Business Interest Deduction	163(j)	-3.1	-3.7
Link up to More Generous Expensing of Depreciable Assets	179	-0.9	-1.9
Link up to Pro-Rata Share Rules	951, 951A	0.0	0.3
Link up to Charitable Deductions for Corporations	170(b)(2)(A), (d)(2)	0.0	0.5
Link up to Miscellaneous Business and Corporate Provisions		0.7	0.8
Decouple from Domestic R&E	174(a)	5.5	5.8
Decouple from Special Depreciation for Qualified Production Property	168(n)	-	-
Decouple from Qualified Small Business Stock Gain Exclusion	1202(a)(1)	-	2.7
Decouple from Section 250 Deduction	250(a)	-	14.6
Downtown and Village Tax Credit Increase by \$2M		-2.0	-2.0
Research & Development Credit Increase to 75%		-	-7.8
<b>Total</b>		<b>0.2</b>	<b>8.3</b>



# Questions?

