

Federal Tax Reform: Its Impact on NC Tax Revenues

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Congress recently enacted significant tax legislation that takes effect in 2018. States whose tax calculations mirror federal tax calculations must decide whether to conform or not conform to the many federal tax changes. The legislation's impact on North Carolina will not be as significant as it may be on other states due to the tax reform changes enacted in this State since 2011. Here are some of the major tax reform changes NC has enacted that minimize the impact of the federal tax changes:

- NC starts with federal adjusted gross income (AGI) instead of federal taxable income.
- NC does not conform to federal standard deduction or personal exemption amounts.
- NC does not conform to federal itemized deductions.
- NC allows cost of capital asset purchases to be deducted over a five-year period in place of federal law that allows the cost to be deducted in one year.
- NC eliminated tax credits that were based on federal tax credits.

The major federal tax changes include the following:

- Changes in individual and corporate tax rates. – NC sets its own tax rates.
- Elimination of personal exemptions and changes to the standard deduction. – NC does not conform to federal personal exemption amounts or standard deduction amounts.
- Elimination of, and changes to, numerous itemized deductions. – NC does not conform to federal itemized deductions.
- Change to bonus depreciation and Section 179 expensing. – NC does not conform to these federal tax laws.
- Allowance of a deduction against federal taxable income for certain pass-through business income. – NC begins its tax calculation with federal AGI. The deduction for business income will not change the calculation of AGI.

Although the Central Staff Finance Team does not believe the federal changes will significantly impact NC's overall revenue collections, there will be some provisions that have a fiscal impact. The IRS will be issuing guidance as to how many of these provisions will be administered. How the provisions are administered may affect how NC tax calculations are made and their resulting fiscal impact. The Finance Team continues to evaluate the federal tax changes as it awaits IRS guidance. The General Assembly will need to consider whether to conform or not conform to the federal changes that have a fiscal impact as part of the annual IRC Update legislation it considers during the 2018 Regular Session.