

**ESTIMATED IMPACT ON STATE REVENUES
OF CONFORMITY TO THE REVISIONS MADE
TO THE INTERNAL REVENUE CODE
DURING CALENDAR YEAR 2015**

**Prepared by the
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Office of Economic Research and Analysis
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Pursuant to A.R.S. §42-1005 (A)(5), the Arizona Department of Revenue is directed to “prepare and submit to the legislature a report containing a summary of all the revisions made to the internal revenue code during the preceding calendar year”. The current definition of internal revenue code in A.R.S. §42-1001 and §43-105 includes those changes to the internal revenue code that became effective on January 1, 2015 along with all federal retroactive effective dates, but excluding any change to the code enacted after January 1, 2015.

Since January 2015, there have been several federal acts that made changes to the internal revenue code (see Attachment I for a brief explanation of the major provisions of these acts). For the majority of the provisions, conforming will have negligible revenue impact to Arizona because the changes were due to either a federal tax that is not applicable to Arizona or there was negligible or unknown impact at the federal level. However, certain provisions in the Bipartisan Budget Act of 2015 are likely to have a negative revenue impact to the state. This bill modified partnership audits conducted by the Internal Revenue Service (IRS); while this will have positive revenue impact at the federal level, it will create negative revenue impact as Arizona will no longer be able to identify income from federal adjustments of partnership income.

Additionally, the “Protecting Americans from Tax Hikes Act of 2015” made permanent or extended certain expiring tax provisions (see Attachment II). Because Arizona previously conformed to these provisions, conforming to this act will continue current Arizona tax policy.

Attachment I
NEGLIGIBLE OR UNKNOWN REVENUE IMPACTS

Slain Officer Family Support Act of 2015:

Extends the tax deadline so that individuals making charitable donations to organizations supporting the families of assassinated New York Police Department (NYPD) Detectives Wenjian Liu and Rafael Ramos can apply such tax deductions to their 2014 tax return. Clarifies that these donations qualify as charitable contributions for tax purposes, and payments by charitable organizations to the family of the two officers will be treated as related to the organizations exempt purpose.

- Effective Date: *2014 and 2015 tax years.*
- Revenue Impact: Likely minimal because it applies to only two families.

Don't Tax Our Fallen Public Safety Heroes Act

Provides that certain compensation paid to public safety officers and their dependents due to death or disability in the line of duty is not subject to federal income tax.

- Effective Date: *on enactment 5/22/2015.*
- Revenue Impact: This change can potentially decrease Arizona's starting point for calculating Arizona tax which would reduce the total Arizona individual income tax collections. According to the Officer Down Memorial web page, 116 officers died in the US in 2015 through the end of November (zero in AZ). In 2014 the number was 133 in the US (3 in AZ).

Defending Public Safety Employees' Retirement Act:

Adds federal law enforcement officers, firefighters and air traffic controllers to the government plans that can retire at 50 instead of 55 without a 10% federal tax on distributions made after 59 and 1/2.

- Effective Date: *Distributions after 12/31/2015.*
- Revenue Impact: N/A.

Trade Preferences Extension Act of 2015:

Modifies health coverage tax credit and child tax credit, requires payee statements for the education credits or deduction for qualified tuition, changes the time for payment of certain corporate estimated taxes, and increases information return and payee statement penalties.

- Effective Date: *various effective dates depending on provisions.*
- Revenue Impact: Mostly not applicable to the state. If fewer taxpayers claim the education deduction due to the enhanced reporting requirement then state individual income tax collections could increase.

Surface Transportation and Veterans Health Care Choice Improvement Act of 2015:

Modifies tax return due dates: federal partnership due dates will change from the 15th day of the 4th month to the 15th day of the 3rd month, C-Corporation return due dates will change from the 15th day of the 3rd month to the 15th day of the 4th month.

Also modifies certain provisions related to highway trust funds and excise taxes, increases amount of information that is required to be reported regarding mortgage statements, adds requirements for consistent basis reporting for estate tax, clarifies that extended six-year statute of limitations applies to a case in which there is an "overstatement of basis", makes changes to health coverage for veterans.

- Effective Date: *various.*
- Revenue Impact: Negligible.

Bipartisan Budget Act of 2015:

Changes the way the IRS handles partnership audits and administers income adjustments. Currently, if the IRS audits a large partnership, the adjustments are looked at the partnership level and then the IRS issues an assessment to each partner. This process made many partnership audits very costly. Under the new law, the IRS will assess an imputed tax to the partnership and will not have to assess each partner (an exception is made for partnerships with less than 100 partners).

- Effective Date: *Generally, partnership tax years beginning after 12/31/2017. However, a partnership may elect to have the new law apply any time after enactment (11/2/2015) or as prescribed by the Secretary of the Treasury.*
- Revenue Impact: Negative revenue impact. This change creates administrative problems and a loss of revenue for the state. Since each partner's federal income tax return will not be not adjusted by the IRS, the partner's federal adjusted gross income (which is Arizona's starting point) will also not be not adjusted. As a result, Arizona will not be able to piggy back a federal audit or amended return of the partner and Arizona will no longer be able to pick up the income from federal adjustments of partnership income. The exact impact is not determinable.

Fixing America's Surface Transportation Act

Deals with trust funds and excise taxes, reforms the rules relating to the IRS using third party qualified tax collection entities, sets up a special compliance personnel program account, allows for hiring of field collection officers. Also provides for the revocation or denial of passports in the case of certain seriously delinquent tax debt (not part of conformity).

- Effective Date: N/A.
- Revenue Impact: N/A.

Every Student Succeeds Act:

Conforming amendments due to changes in other laws.

- Effective Date: 2016.
- Revenue Impact: Minor, if any.

Consolidated Appropriations Act of 2015:

Contains the following provisions: delays the excise tax on high cost, employer-sponsored health coverage until 2019 from 2017; allows taxpayer to take a deduction on their federal income tax for the excise tax on high cost employer-sponsored health coverage; extension and phaseout of credits for wind facilities; election to treat qualified facilities as energy property; extension and phaseout of solar energy credit; extension and phaseout of credits with respect to qualified solar electric property and qualified solar water heating property; treatment of transportation costs of independent oil refiners, allows a more beneficial treatment of costs.

- Effective Date: *various.*
- Revenue Impact: Excise tax deductions will increase the amount that can be deducted for Arizona purposes, therefore will reduce Arizona taxable income (excise tax is delayed until 2019 so no cost will be incurred by AZ until 2019). Treatment of oil refiners cost will reduce taxable income reported to Arizona for any independent oil refiners that file to Arizona.

Attachment II
EXTENSION OF EXPIRING TAX PROVISIONS
Protecting Americans from Tax Hikes Act of 2015

(\$ in millions)	FY2016	FY2017	FY2018	FY2019
Extension of Expiring Tax Provisions ¹	(\$51.5)	(\$70.6)	(\$28.2)	(\$34.5)

Extension of Expiring Tax Provisions:

The Protecting Americans from Tax Hikes Act deals with extending various tax provisions.

The provisions made permanent include:

- Deduction up to \$250 for teacher classroom expenses (starting 2016, the \$250 limit is annually adjusted for inflation)
- Itemized deduction for state and local sales taxes
- Tax-free distributions from IRAs to charities for individuals age 70-1/2 and older
- 15 year straight line cost recovery for qualified leasehold improvements
- Increased expensing limitations and treatment of certain section 179 properties
- Reduction in S-corporation recognition period for built-in gains

Other extended provisions include:

- Discharge of indebtedness on principal residence
 - Itemized deduction for mortgage insurance premiums
 - Deduction for qualified tuition related expenses
 - Special expensing rules for certain film and television productions
 - Bonus Depreciation (impacts Arizona by individual taxpayers subtraction for 10% of federal bonus depreciation)
- Effective Date: *Generally taxable years beginning after December 31, 2014.*
 - Revenue Impact: Generally decreases tax revenue.

Extension of Expiring Tax Provisions: Tax Credits

Several of the federal credits may have an impact on state tax revenue through reduced federal deductions from a change in the amount of expenses allowed/disallowed, or when a sale occurs and the taxpayer's basis in the property is reduced.

- R & D credit
 - Alternative fuel vehicle refueling property
 - Credit for biodiesel and renewable biodiesel
 - Credit for renewable power facilities
 - New markets tax credit
 - Railroad track maintenance
 - Work opportunity tax credit
 - Construction of energy efficient new homes
 - Indian employment tax credit
- Effective Date: *Generally taxable years beginning after December 31, 2014*
 - Revenue Impact: Generally a potential increase in revenue.

In addition to the tax extenders, the Protecting Americans from Tax Hikes Act contains provisions to strengthen the integrity of tax credit programs, reform the Internal Revenue Service, and includes miscellaneous provisions related to family tax relief, real estate investment trusts and others. The miscellaneous provisions will have a minimal revenue impact to the state, which is included in the figures above.

¹ Generally Arizona previously conformed to these provisions, thus conforming to this act will continue current Arizona tax policy.