Model Review: Corporate Income/Net Receipts Tax, Tax Cuts and Jobs Act Provisions

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Model Purpose	This is a component of the corporate income/net receipts tax model (Corporate Macro Model). Refer to "Model Review: Corporate Income/Net Receipts Tax Macro Model" (the CIT Model Review document) for details on the purpose.
Data Sources	We use the following data sources to model the impact of the Tax Cuts and Jobs Act (TCJA) provisions: Federal Tax Collections • Internal Revenue Service (IRS) aggregate data;[1] • US Department of Treasury press release.[2] Federal Tax Credits and Deductions • IRS Statistics of Income (SOI) data;[3] • IRS Microdata for Washington federal corporate income tax (FTI).[4] Impact of Federal Tax Reform on Tax Credits and Deductions (2018-19) • Joint Committee on Taxation (JCT);[5] Growth Projections/Conversions of Annual Data to Quarterly • Bureau of Economic Analysis (BEA), Before tax Corporate Profits;[6]
Requirements Model Used to Fulfill	This is a component of the Corporate Macro Model. Refer to the CIT Model Review Document for details on the requirements fulfilled by the model.

[1] This includes the IRS Data Book (various years through 2018) and IRS Statistics of Income (SOI) data (various years through 2018).
[2] US Treasury Department, *Mnuchin and Vought Release Joint Statement on Budget Results for Fiscal Year 2019*.
[3] Corporation income tax return line item estimates (2008 through 2016).
[4] Federal tax information: Internal Revenue Service (2017). *Business Master File (BMF) and Business Return Transaction File (BRTF) Extracts Specification Book*: Extract Year (EY) 2017.
[5] Joint Committee on Taxation. *Estimated Budget Effects of the Conference Agreement for H.R. 1, the 'Tax Cuts and Jobs Act*, December 2017.
[6] Bureau of Economic Analysis Forecast Statistic: Before-tax corporate profits with IVA & capital consumption adjustment, billions of dollars. (Various years). (Compiled by Washington Economic and Revenue Forecast Council.)

Questions for Technical Advisory Group	The following are questions for the Technical Advisory Group: 1. What is a reasonable estimate of (or way of estimating) the average foreign tax rate on deemed repatriated foreign earnings of US corporations? (This tax rate is likely relatively low, because pre-TCJA, there was a stronger incentive for taxpayers to avoid repatriating earnings from low tax jurisdictions.) 2. For all analyses, we welcome suggestions relating to data sources, background reading, and methods.
Questions from Technical Advisory Group	*We will capture at meeting and record here*

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Overview

In December 2017, President Trump signed the TCJA into law. This legislation included a reduction of the corporate income tax rate from 35% to 21% and a myriad of other provisions that dramatically changed the US corporate income tax structure. Most of the provisions of the TCJA went into effect January 1, 2018.

Under ESHB 1109 (2019) Sec. 137, the Department must estimate the revenue impacts of a corporate income/net receipts tax during Washington's 2017-19 fiscal biennium, a period which includes the enactment of the TCJA. Unfortunately, only limited federal tax data is available after the enactment of the TCJA to identify its impact on federal corporate taxable income, the starting point for the proposed Washington corporate income/net receipts tax. Therefore, in the absence of direct data, it was necessary for the Corporate Macro Model to incorporate estimated or inferred impacts of the TCJA. This report supplements the CIT Model Review document by describing the modeling of the TCJA provision impacts.[7]

- Using SOI macro data through 2016, we first modeled a counterfactual in which the tax structure remained unchanged during the US Fiscal Years (FY) 2016-2019.
    - This included inferring quarterly estimates from annual data.[8]
- Next, primarily using JCT's December 2017 forecasts of the projected budget impacts of the TCJA provisions, we modeled the tax structure for calendar years 2018 and 2019, including tax reform changes.
- Finally, we reconciled the modeled tax structure with actual tax collections through US FY 2019. We attributed the model's ***over***estimation of tax collections in US FY 2018 and slight ***under***estimation of collections in US FY 2019 to misestimated tax deductions in the two years. We adjusted the model accordingly.[9]

Model Background

The CIT Model Review document describes the steps involved in the Corporate Macro Model. The approach to estimating Washington revenues generated by a corporate income/net receipts tax relies on the following two key equations:

Equation 1

$$Taxable_{US} = \frac{TaxDue_{US} + Total\ Credits_{US} - Alternative\ Taxes_{US}}{Tax\ Rate_{US}}$$

[7] Refer to Step 3 in the CIT Model Review Document.
[8] Inferring quarterly data was necessary because TCJA went into effect in the second quarter of the US Fiscal Year 2018 while the US Treasury Department (including the IRS) reports tax collections data on a fiscal year basis.
[9] Since increasing deductions reduces taxable income – the starting point of the proposed Washington corporate income/net receipts tax – this is a more conservative approach than attributing any residual to misestimated credits or alternative taxes.

Equation 2

$$TaxDue_{Wa} = Tax\ Rate_{Wa} \times Apportionment\%_{Wa} \times Taxable_{US}$$

The portion of the model described in this report allows us to estimate Equation 1Equation 1 (US taxable income). Work related to Equation 2 is ongoing and will utilize the estimates of US taxable income we derive.

Refer to the CIT Model Review Document for additional details on the Corporate Macro Model, including additional background on the corporate income/net receipts proposals in the Gates study (2002).[10]

Tax Cuts and Jobs Act Background

This section describes the major provisions of the TCJA referenced in the description of the TCJA modeling below. In particular, because Tax Credits and Alternative Taxes are components of Equation 1, this section emphasizes provisions that directly or indirectly affect tax credits or alternatives. ***Appendix B*** describes additional significant TCJA provisions.

Reduced corporate tax rate of 21%

Summary: Prior to the TCJA, most federal corporate taxable income was taxed at approximately a 35% rate (with some variation in rates at lower levels of taxable income).[11] The TCJA introduced a flat 21% corporate income tax rate.

Pre-TCJA Corporate Income Tax Schedule (2017):

Taxable Income Range	Marginal Tax Rate	Average Tax Rate[12]
$0 - $50,000	15%	15.0%
$50,000 - $75,000	25%	18.3%
$75,000 - $100,000	34%	22.3%
$100,000 - $335,000	39%	34.0%
$335,000 - $10 million	34%	34.0%
$10 million - $15 million	35%	34.3%
$15 million - $18.33 million	38%	35.0%
$18.33 million +	35%	35.0%

[10] Gates, W.H. (2002). *Tax alternatives for Washington State*. Washington State Tax Structure Committee.
[11] Based on SOI data, we estimate an average tax rate of between 34.7% and 34.8% in most years prior to TCJA.
[12] The average tax rate applies to taxpayers at the top of a given tax bracket.

JCT Estimated Budget Impact:

FY 2018	FY 2019	FY 2018-27
-$101.3 billion	*-$125.3 billion*	*-$1.35 trillion*

Modelling Notes:

Based on the annual tax collections prior to FY 2018, a reduction in the corporate income tax rate to 21% should seemingly lead to a somewhat larger negative budget impact than the JCT estimate suggests. However, JCT's estimated budget impacts can be reconciled by a partially offsetting reduction in tax credits claimed.

There are two reasons a lower tax rate reduces tax credits. First, tax credits generally cannot reduce income taxes below zero.[13] Therefore, under a lower tax rate, some less profitable corporations will reach the limit on the amount of credits they can claim. Second, a lower US tax rate will specifically reduce the amount of foreign tax credits that corporations can claim, since foreign tax credits offset US taxes up to the amount that would have been paid if the income had been earned in the US. In the model described below, we directly reduce the tax rate to 21%, and then infer that there is an offsetting reduction in foreign tax credits such that the net budget impact is equal to the JCT estimate.

Tax on deemed repatriation of foreign income

Summary: The TCJA tax on deemed repatriation of foreign income (the Deemed Repatriation Tax) is a one-time tax on the unrepatriated assets held by foreign affiliates as of the end of 2017.[14]

New Tax Base: The Deemed Repatriation Tax applies to yet untaxed earnings held as assets by foreign subsidiaries of US multinationals. Under pre-2017 law, income of foreign subsidiaries was not taxable until repatriated (e.g., as dividends) to the parent.[15] The Deemed Repatriation Tax was devised to capture unrepatriated foreign earnings as of 2017 (in some cases to avoid US taxation).

Tax Rate: A preferred tax rate of 8% applies to foreign earnings that are deemed repatriated if the foreign earnings were held as working capital as of December 2017. A tax rate of 15.5% applies to deemed repatriations if the foreign earnings were held as cash or cash equivalents. (Legislators considered high foreign cash holdings a proxy for tax avoidance.)

Installments: Taxpayers have the option of paying tax on deemed repatriations in installments over eight years.

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[13] Except in the narrow case of refundable tax credits.

[14] Under TCJA, future dividends paid by foreign subsidiaries to US multinational parents are no longer subject to US taxation (see ***Deductions for dividends received from foreign corporations)***.

[15] Consistent with a move to a territorial system, active income earned by foreign affiliates of US multinationals and repatriated to the US generally is no longer subject to US, with the exception of certain inclusions for low-taxed foreign income (see **Base Erosion Abuse Tax (BEAT)** and **Global Intangible Low-Taxed Income (GILTI)** provisions of the TCJA.

JCT Estimated Budget Impact:

FY 2018	FY 2019	FY 2018-27
+$78.6 billion	+$49.6 billion	+$338.8 billion

Characterization of provision: New alternative tax.[16]

Modelling Notes: Corporations can claim foreign tax credits on deemed repatriations. The JCT estimated budget impact nets the positive budget impact of deemed repatriation against the negative budget impact of increased foreign tax credits. Our model therefore requires as assumption about the average foreign tax rate on deemed repatriations.

Technical Advisory Group Question 1

What is a reasonable estimate of (or way of estimating) the average foreign tax rate on deemed repatriated foreign earnings of US corporations? (This tax rate is likely relatively low, because pre-TCJA, there was a stronger incentive for taxpayers to avoid repatriating earnings from low tax jurisdictions.)

Deduction for dividends received from foreign corporations

Summary: Beginning in the FY 2018, most active income earned by foreign affiliates of US multinationals and paid to the US domestic corporation through a dividend is eligible for a deduction (the Dividends Received Deduction). In effect, this moves the US toward a territorial tax system where US corporations (usually) only pay corporate income taxes on income earned in the US.

Key Exceptions: This deduction does not apply to Subpart F (passive) income or Global Intangible Low-Taxed Income (see ***Global Intangible Low-Taxed Income*** in ***Appendix B***).

JCT Estimated Budget Impact:

FY 2018	FY 2019	FY 2018-27
-$17.8 billion	*-$28.1 billion*	*-$224.0 billion*

Characterization of provision: New Special Deduction.[17]

Model Notes: Although this does not directly change foreign tax credit rules, foreign tax credits become moot in many cases where taxpayers can fully deduct their foreign income. However, as noted in ***Key Exceptions*** above, domestic corporations cannot claim all dividends received from foreign corporations as a deduction.

[16] See Line 32 of Form 1120.
[17] See Schedule C of Form 1120.

We used the ratio of 2018 foreign tax credits to 2017 foreign tax credits among taxpayers with available FTI data in 2017 and 2018[18] to infer the amount foreign tax credits in the macro data.

Changes to Bonus Depreciation (100% Expensing Depreciation of Qualified Property)

Summary: Under the TCJA, bonus expensing (immediate deduction) is allowed on business equipment acquired and placed in service between 2018-26, including 100% expensing for 2018-2022.

Bonus Depreciation Schedule: Bonus expensing of business equipment is allowed at the following rates for 2018-2026:

- ***2018-2022***: 100% Expensing
- ***2023***: 80% Expensing
- ***2024***: 60% Expensing
- ***2025***: 40% Expensing
- ***2026***: 20% Expensing

Pre-2017 Law: Prior to the TCJA, the bonus deduction schedule was 50%, 40%, and 30% for property placed in service in 2017, 2018, and 2019, respectively.

JCT Estimated Budget Impact:

FY 2018	FY 2019	FY 2018-27
-$32.5 billion	*-$36.5 billion*	*-$86.3 billion*

Characterization of provision: Increase in Total Deductions.

Base Erosion and Anti-abuse Tax (BEAT)

Summary: The Base Erosion and Anti-abuse Tax (BEAT) is an alternative minimum tax that is calculated similar to regular corporate income tax liability, except that: i) certain deductions such as those taken for most payments to foreign affiliates are disallowed, and ii) a lower tax rate applies. If a taxpayer's BEAT tax calculation is greater than its regular corporate income tax liability, the taxpayer must pay the tax liability under BEAT.[19]

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[18] Only a subset of 2018 FTI data is available. Therefore, the comparison between 2017 and 2018 foreign tax credits is based only on taxpayers appearing in both years' data.

[19] Most payments to foreign affiliates are disallowed and hence added back to determine the taxpayer's modified taxable income (MTI) and any alternative BEAT tax liability. Payments to foreign affiliates that qualify as COGS or that qualify under §482-9 for the Services Cost Method are exceptions, and do not need to be added back to determine MTI.

Threshold: Corporations with average annual gross receipts greater than $500 million in the 3-year tax period preceding the current tax year.

Tax Rate: The applicable BEAT tax rate schedule is as follows:

- ***2018***: 5%
- ***2019-2025***: 10%
- ***2026-***: 12.5%

JCT Estimated Budget Impact:

FY 2018	FY 2019	FY 2018-27
+$0.8 billion	+$4.3 billion	+$149.6 billion

Characterization of provision: New alternative tax.

Approach

As noted in the ***Overview*** section, we modeled the impact of the TCJA provisions as follows:

- Using SOI macro data through 2016, we first modeled a counterfactual in which the tax structure remained unchanged during US FY 2016-2019.
- Primarily using JCT's December 2017 forecasts of the projected budget impacts of the TCJA provisions, we then modeled the tax structure for calendar years 2018 and 2019, including tax reform changes.
- Finally, we reconciled the modeled tax structure to account overestimation or underestimation of actual corporate income collections through US FY2019.

This section elaborates on those steps.

Modeling Counterfactual with No Changes to Tax Structure

Initial Data

Our model of the impacts of the TCJA provisions begins with 2008-2016 SOI line item estimates of:

- Total Income (Form 1120, Line 11),
- Special Deductions (Form 1120, Line 29b)
- NOLs and Special Deductions (Form 1120, Line 29c)[20]

[20] Because the SOI Line Item estimates are based on an 80% sample, there is a sampling error associated with the estimates. As such, some axiomatic equations do not quite hold when utilizing all line item estimates as reported. To ensure such equations held, we backed out certain line item using the equations shown below:

- Total Deductions = [Total Income] – [NOL and Special Deductions]

- Taxable income (Form 1120, Line 30),
- Total Tax (Form 1120, Line 31),
- Income Tax, Pre-Credits (Schedule J, Line 2),
- Alternative Minimum Tax (Schedule J, Line 3),
- Foreign Tax Credits (Schedule J, Line 5a),
- General Business Credits (Schedule J, Line 5c), and
- Total Non-Refundable Credits (Schedule J, Line 10).

Because Washington's Fiscal Year begins July 1, the US Fiscal Year (and collections data) begins October 1, and the TCJA was enacted on January 1, modelling is ultimately intractable without converting annual data to quarterly data. Therefore, although the SOI line item estimates data are based on tax years, we convert the annual line item estimates into four quarterly line item estimates by multiplying them by: $\frac{Quarterly\ Corporate\ Profits}{Annual\ Corporate\ Profits}$.[21]

Projecting US FY 2017 Aggregate Data

We rely on IRS reported (actual) tax collections data for US FY 2008-2019 to project the data beyond US FY 2016.[22] For each quarter through US FY 2016, we calculate:

- Total Income,
- All deduction line items,
- All tax credit line items, and
- Alternative Tax

as a percentage of the same quarter's tax collections. We then take a three-year average of such ratios and apply that to US FY 2017 tax collections to determine line item estimates for US FY 2017 (e.g.,

$$Total\ Credits_{2017} = Avg\left(\frac{Total\ Credits}{Total\ Collections}\right)_{2014-16} \times Total\ Collections_{2017}$$

For each year in the period FY 2008 – FY 2016, the computed average tax rate (Total Tax Before Credits / Taxable Income) was between 34.69% and 34.82%. We applied the 5-year average (FY 2012 – FY 2016) tax rate of 34.77% to FY 2017. We then completed the model for US FY 2017 by computing the following.

Equation 3

$$Taxable\ Income\ = Total\ Income - Total\ Deductions - Special\ Deductions - NOLs$$

- Total Credits = [Income Tax, Pre-Credits] – [Total Tax] + [Alternative Minimum Tax]
- NOLs = [NOLs and Special Deductions] – [Special Deductions]
- Total Refundable Credits = [Total Credits] – [Total Non-Refundable Credits].

[21] BEA Estimates.

[22] We converted tax collections amounts from annual to quarterly data in the same manner as line item estimates, as described above.

Equation 4

$$Income\ Tax\ Pre-Credit\ =\ Avg\ Tax\ Rate\ \times\ Taxable\ Income$$

Equation 5

$$Total\ Tax\ =\ Income\ Tax\ Pre-Credit\ +\ Alternative\ Taxes-\ Total\ Credits$$

Projecting FY 2018 – 2019 Counterfactual Data

To construct FY 2018 – FY 2019 data that simulates a US FY 2018-19 counterfactual world with no TCJA, we scaled up the US FY 2017 quarterly estimates of total income, individual deductions, individual credits, and alternative taxes based on the growth of corporate profits[23] in the same period.[24]

Modeling the TCJA Provisions

We relied primarily on the JCT (2017) estimates of the budget impacts of the TCJA provisions to incorporate their effects into the model. We included all provisions affecting C-Corporations with a non-zero budget impact in FY 2018 and FY 2019. This included:

- The reduction in the tax rate,
- 43 provisions affecting taxable income (primarily deductions, some affecting total income),
- Three reduced or eliminated credits,
- Two new alternative taxes and the repeal of an existing alternative tax

In most instances, we simply modeled these budget impacts as follows:[25]

Type of Provision	Budget Impact[26]	Implementation in Model
Total Income	$+X$	Increase Total Income By $\frac{X}{.21}$
Deduction	$-X$	Increase Deductions By $\frac{X}{.21}$
Credit	$-X$	Increase Credits by X
Alternative Tax	$+X$	Increase Alternative Taxes by X

[23] BEA estimates.
[24] We used corporate profit growth between FY 2017 quarter 1 and FY 2018 quarter 1 to construct line item estimates for FY 2018 quarter 1. (Likewise, we do the same for each subsequent quarter through US FY 2019 quarter 4.)
[25] For the opposite type of provision (a decrease rather than increase), merely reverse the signs.
[26] We adjusted the budget impacts of some provisions downward to account for some of the budget impact relating to S-Corps or businesses other than C-Corps. The JCT budget impacts do not generally distinguish between the budget impacts related to C-Corps vs. other types of businesses. For provisions not limited to C-Corps, we assumed 90% of the budget impact related to C-Corps for international provisions and we assumed 75% of the budget impact related to C-Corps for other provisions.

With each modeled provision, we also made corresponding changes to Taxable Income, Income Tax (Pre-Credit), and Total Tax to ensure that ***Equation 3*** - ***Equation 5*** continued to hold.

TCJA Provisions Requiring Non-Standard Implementation in Model

Reduction in Tax Rate

The model can compute the direct budget impact of the reduction in tax rate by simply changing the tax rate in the counterfactual model and calculating the change in the income tax. This results in a somewhat larger negative calculated budget impact than the JCT estimates. As alluded to above, this is explainable because the reduced tax rate also causes a corresponding decrease in tax credits, especially foreign tax credits, which partially offsets the lost income from the reduced tax rate.[27] Therefore, we reduce foreign tax credits by the difference between the two estimates of the budget impact of the tax reduction.

Deemed Repatriation Tax

Corporations can claim foreign tax credits on deemed repatriations. The JCT estimated budget impact nets the positive budget impact of deemed repatriation against the negative budget impact of increased foreign tax credits. To estimate the effect on foreign tax credits, our model requires an assumption about the average foreign tax rate paid on earnings under the Deemed Repatriation Tax. We have not yet modeled any offsetting increase in foreign tax credits.

Dividends Received Deduction

Under the TCJA, except in cases of passive income or low taxed income, corporate taxpayers can now fully deduct dividends received from foreign affiliates. Thus, a significant amount of foreign tax credits become moot because of the dividends received deduction. As with the previous two provisions discussed above, the budget impact of the Dividends Received Deduction includes an offsetting change in foreign tax credits.

In an effort to estimate the final amount of foreign tax credits for FY 2018 and FY 2019, we turned to FTI data. Specifically, we decreased foreign tax credits (and correspondingly increased special deductions)[28] in both FY 2018 and FY 2019 of our model to align with the aggregate ratio of 2018 foreign tax credits to 2017 foreign tax credits in FTI data. Only a subset of 2018 FTI data is available. Therefore, the comparison between 2018 and 2017 foreign tax credits is based only on taxpayers appearing in both years' data.

The graphs on the following pages depict the tax structure of the counterfactual (no TCJA) model, alongside the model with the TCJA provisions implemented.

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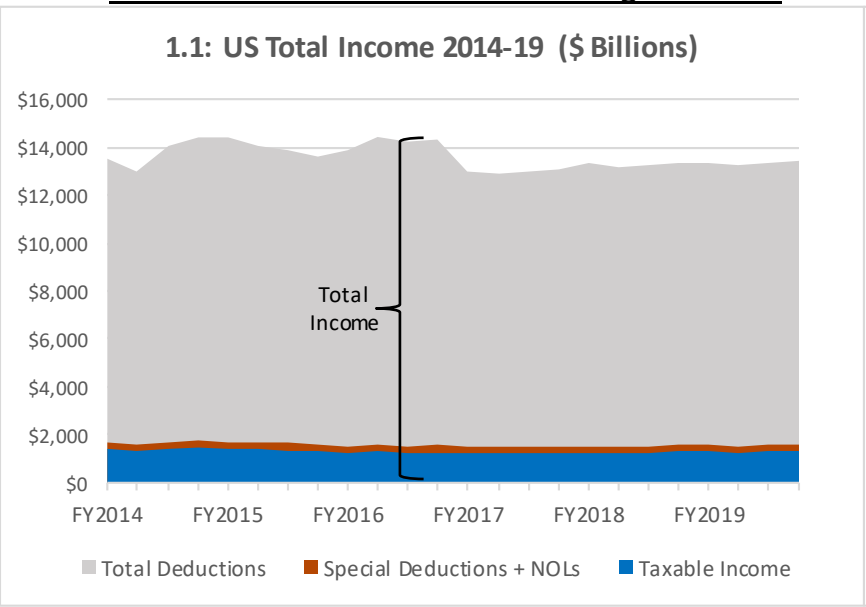
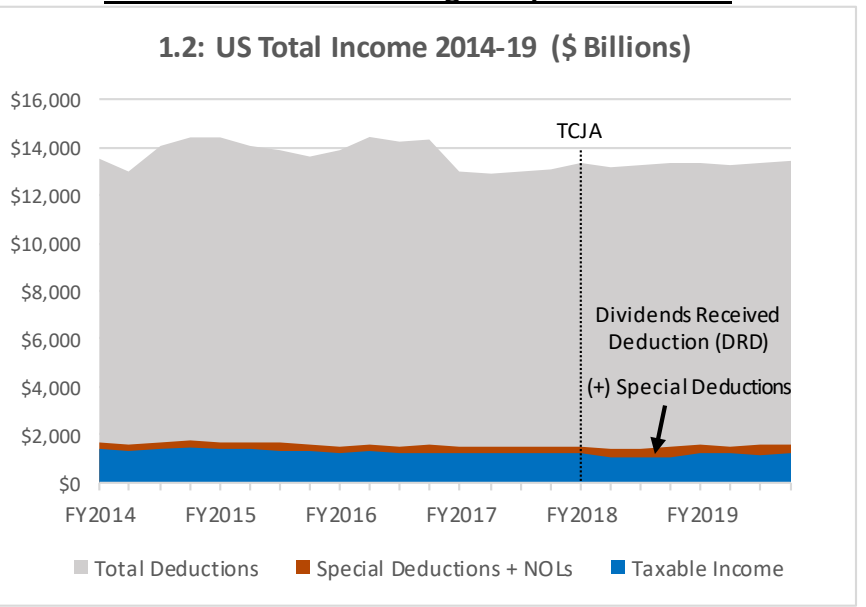
[27] There are two reasons a lower tax rate reduces tax credits. First, tax credits generally cannot reduce income taxes below zero. Therefore, under a lower tax rate, some less profitable corporations will reach the limit on the amount of credits they can claim. Second, a lower US tax rate will specifically reduce the amount of foreign tax credits that corporations can claim, since foreign tax credits offset US taxes up to the amount that would have been paid if earnings occurred in the US.

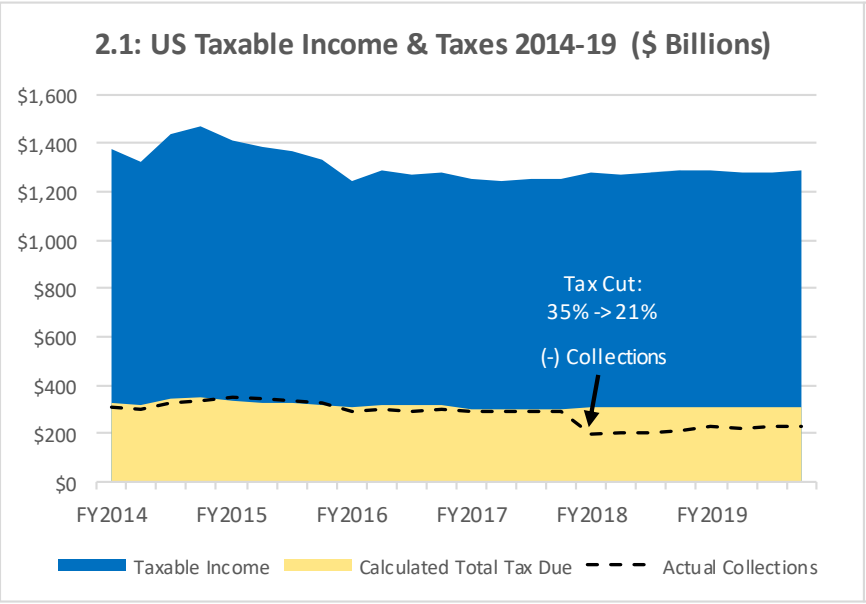
[28] Dividends received deductions are characterized as a special deduction.

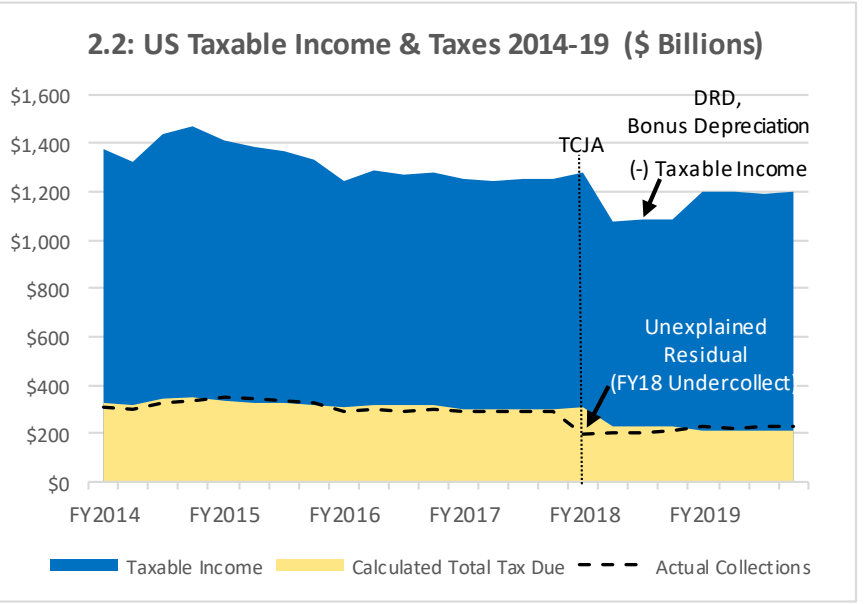
Counterfactual: No Tax Structure Change Modeled

JCT Estimates of TCJA Budget Impacts Modeled



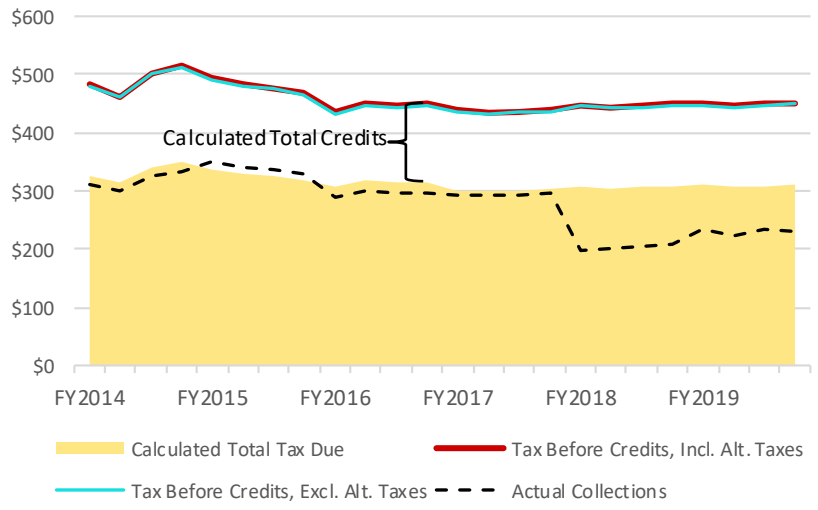


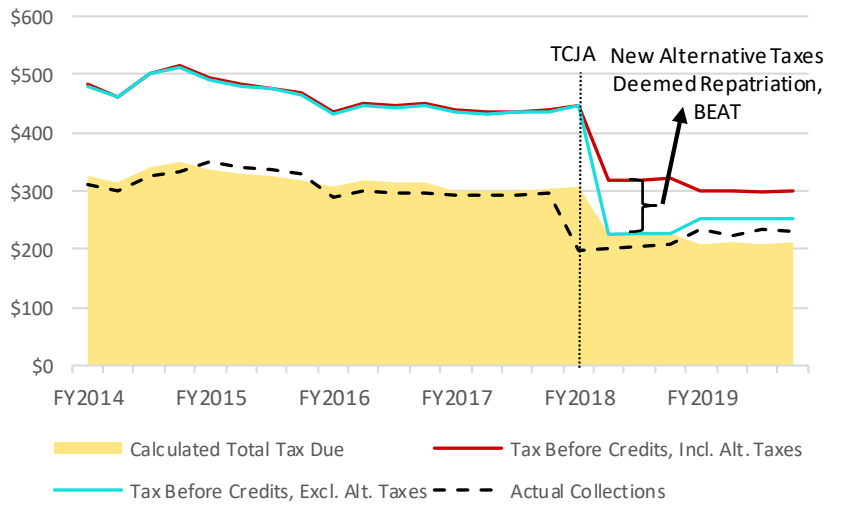


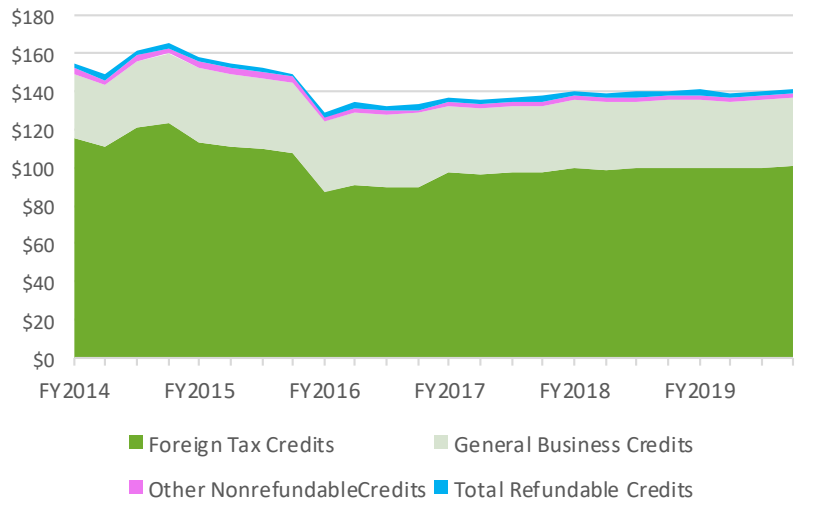


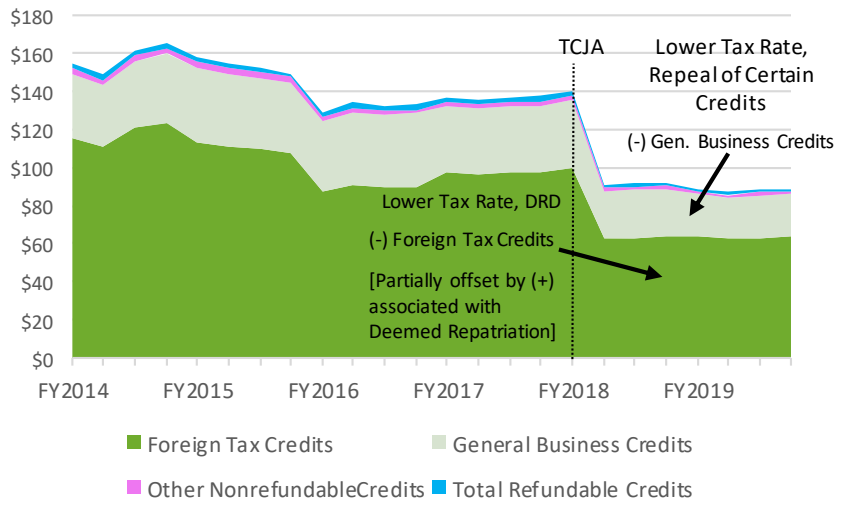
Counterfactual: No Tax Structure Change Modeled

JCT Estimates of TCJA Budget Impacts Modeled









Reconciliation of Model to Actual Collections

As can be most clearly seen by comparing Graph 3.1 and 3.2 above, the modelling of the TCJA provisions significantly reduces the gap between the model's calculated total tax vs. actual tax collections per IRS data. However, as it stands the model still overestimates total tax for FY 2018 and slightly underestimates total tax for FY 2019. This gap is consistent, though, with reports of unexplained weakness in corporate income tax collections. For example, the Congressional Budget Office's (CBO) 2019 Budget Outlook stated:

"Corporate tax collections in 2017 and early 2018 were weaker than can be explained by currently available data on business activity. CBO anticipates that factors responsible for that weakness (which will not become apparent until information from tax returns becomes available over the next two years) will gradually dissipate over the next several years."

Given the sheer number and scale of changes to corporate income taxes under TCJA, it is perhaps unsurprising that the estimates did not perform perfectly immediately after the implementation of the new law. Behavioral changes can be particularly challenging to capture fully. One such behavioral change that could explain weak tax collections in US FY 2018 is the incentive for some taxpayers to accelerate deductions in late 2017.[29] With expected corporate tax cuts on the horizon, many firms surely sought opportunities to reduce their tax burden in the final year of the old, higher tax regime.

The CBO continued:

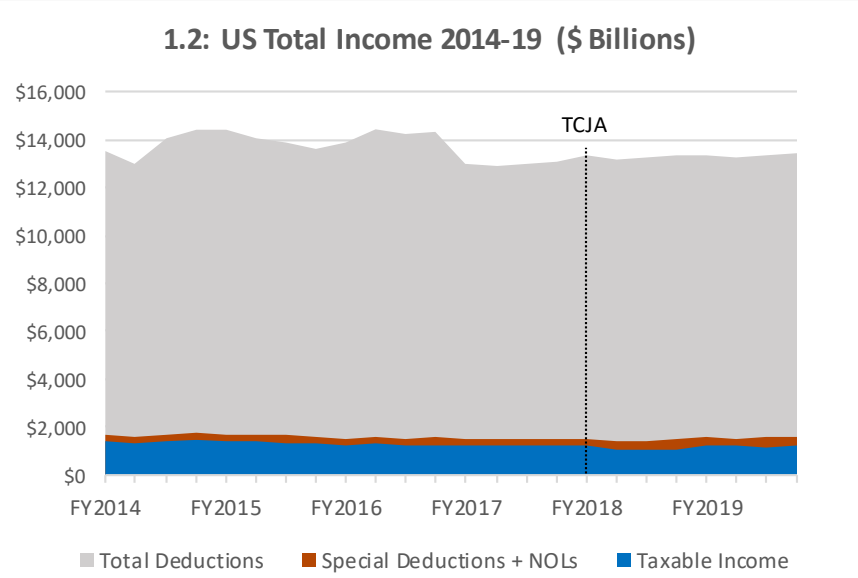
"One effect of the reduction in January 2018 of the corporate tax rate to 21 percent was an incentive for some firms to accelerate expenses. By accelerating expenses, such as employee compensation, they could claim deductions at higher tax rates, thus lowering their tax liabilities in fiscal year 2018. That opportunity, which probably temporarily reduced corporate receipts in 2018, no longer exists."

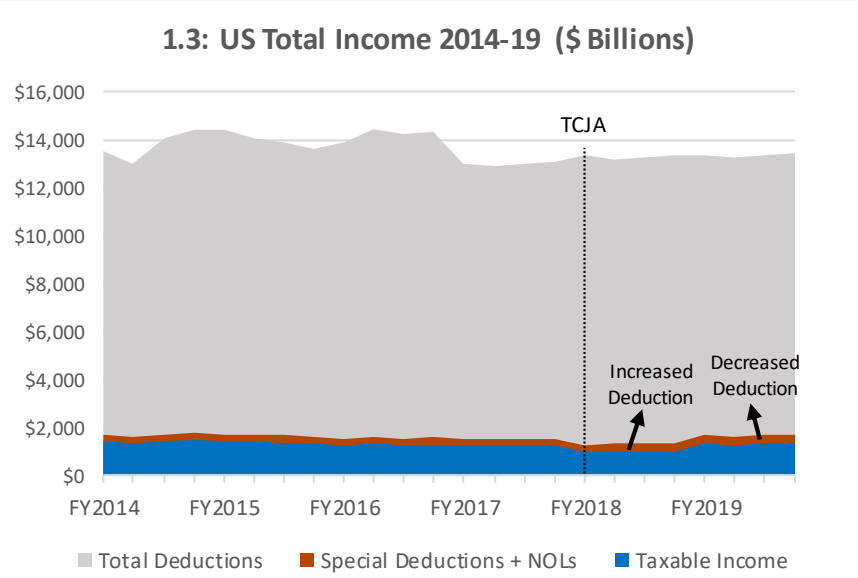
While it is by no means certain that accelerated FY 2018 deductions are the cause of the weakness in FY 2018 corporate tax collections, it is consistent with the somewhat stronger FY 2019 corporate collections we observe. (A corporation that moved up a deductible expense to December 2017 cannot claim the deduction on their 2018 tax return.) Therefore, it is reasonable to attribute the "residual" gaps in collections in FY 2018 and FY 2019 (refer to Graph 2.2 and Graph 3.2) to an underestimation of Total Deductions in FY 2018 and a slight overestimation of Total Deductions in FY 2019. We take this approach and depict the implied changes to the tax structure in the graphs that follow.

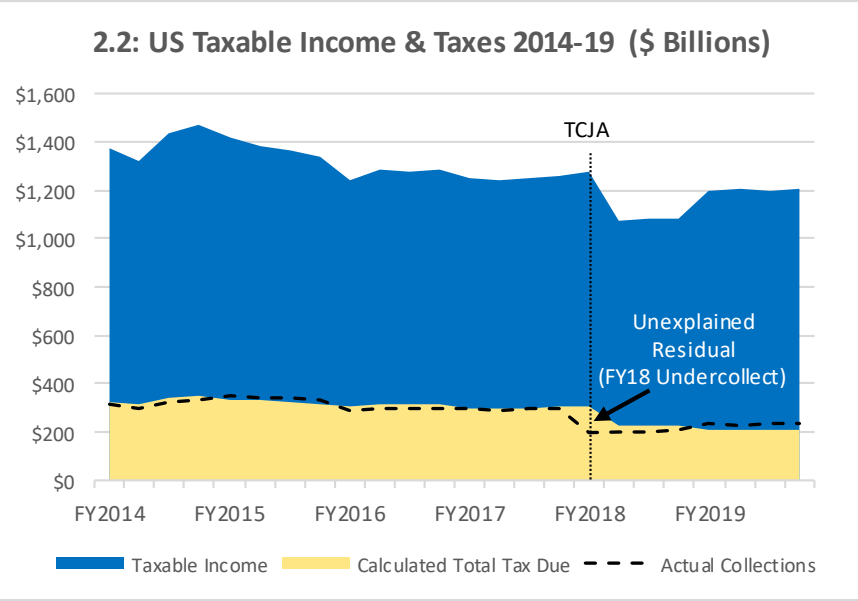
[29] Note that US FY 2018 began October 2017.

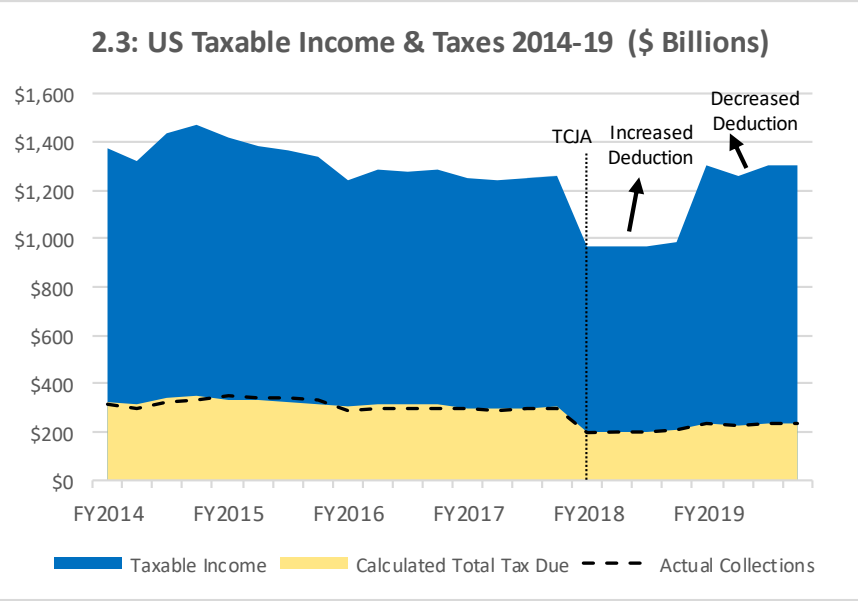
JCT Estimates of TCJA Budget Impacts Modeled

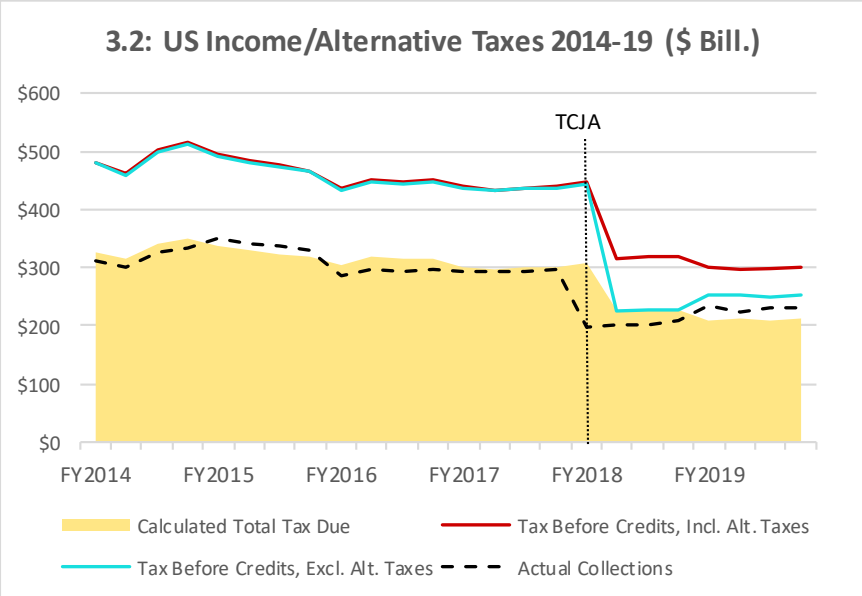
Residuals Reconciled with Changes to Total Deductions

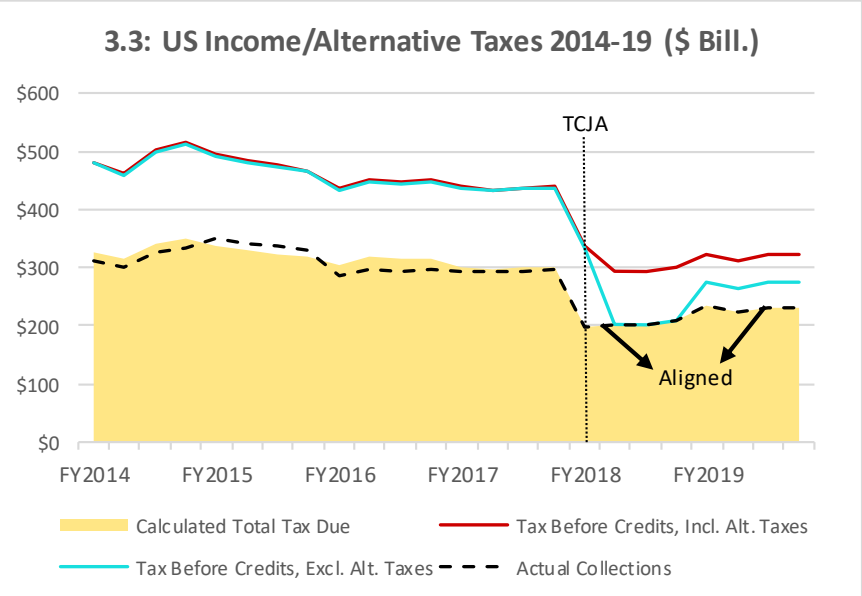


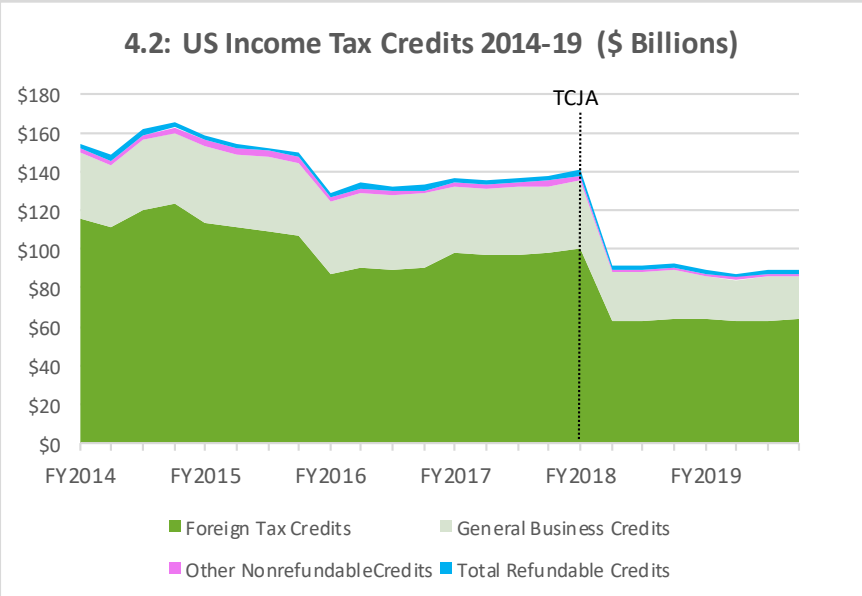


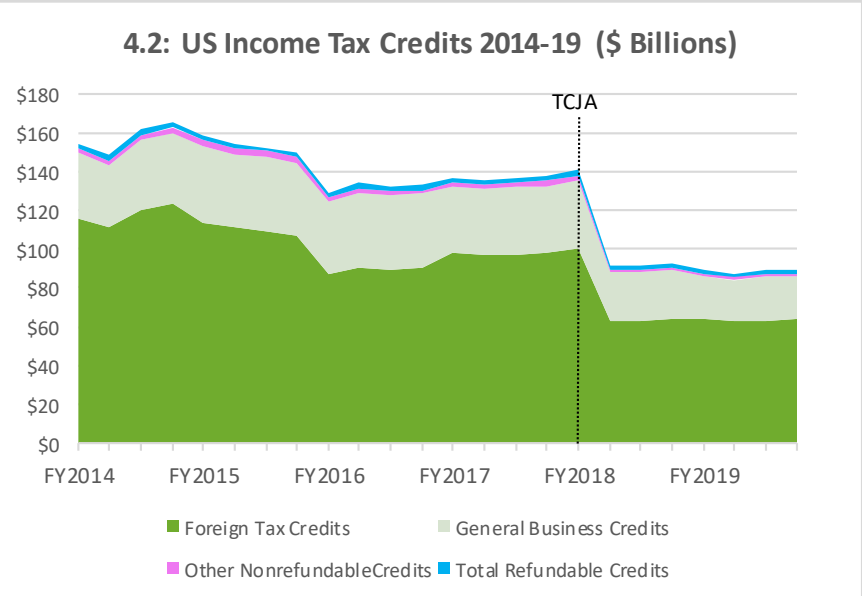





3.2: US Income/Alternative Taxes 2014-19 ($ Bill.)
$600
$500
$400
$300
$200
$100
$0
TCJA
FY2014
FY2015
FY2016
FY2017
FY2018
FY2019
Calculated Total Tax Due
Tax Before Credits, Incl. Alt. Taxes
Tax Before Credits, Excl. Alt. Taxes
Actual Collections


3.3: US Income/Alternative Taxes 2014-19 ($ Bill.)
$600
$500
$400
$300
$200
$100
$0
TCJA
Aligned
FY2014
FY2015
FY2016
FY2017
FY2018
FY2019
Calculated Total Tax Due
Tax Before Credits, Incl. Alt. Taxes
Tax Before Credits, Excl. Alt. Taxes
Actual Collections


4.2: US Income Tax Credits 2014-19 ($ Billions)
$180
$160
$140
$120
$100
$80
$60
$40
$20
$0
TCJA
FY2014
FY2015
FY2016
FY2017
FY2018
FY2019
Foreign Tax Credits
General Business Credits
Other NonrefundableCredits
Total Refundable Credits


4.2: US Income Tax Credits 2014-19 ($ Billions)
$180
$160
$140
$120
$100
$80
$60
$40
$20
$0
TCJA
FY2014
FY2015
FY2016
FY2017
FY2018
FY2019
Foreign Tax Credits
General Business Credits
Other NonrefundableCredits
Total Refundable Credits

Other Questions for the Technical Advisory Group

Technical Advisory Group Question 2
For all analyses, we welcome suggestions relating to data sources, methods, and references.

Ideas from the Technical Advisory Group

- *We will capture these during the meeting*

Appendix A: References

Bureau of Economic Analysis: Statistics/Forecast: *Before-tax corporate profits with IVA & capital consumption adjustment, billions of dollars*. (Various years, as compiled by Washington Economic and Revenue Forecast Council.)

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Internal Revenue Service (2018): *Internal Revenue Service Data Book 2018.* Publication 55b. https://www.irs.gov/pub/irs-pdf/p55b.pdf.

IRS Statistics of Income Division (November 2019). *SOI Tax Stats. Corporation Income Tax Returns. Returns of Active Corporations: Table 3.3: Selected Balance Sheet, Income Statement, and Tax Items, by Size of Business Receipts – 2015.* https://www.irs.gov/statistics/soi-tax-stats-corporation-complete-report.

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Joint Committee on Taxation (2017): *Estimated Budget Effects of the Conference Agreement for H.R. 1, the 'Tax Cuts and Jobs Act, December 2017'*. https://www.jct.gov/publications.html?func=startdown&id=5053.

United States Treasury Department (2019): Press Release: *Mnuchin and Vought Release Joint Statement on Budget Results for Fiscal Year 2019*. https://home.treasury.gov/news/press-releases/sm806.

Washington State Legislature (2018): *House Tax Structure Work Group Final Report.* House report (2018). https://app.leg.wa.gov/committeeschedules/Home/Document/186393.

Appendix B: Additional Tax Cuts and Jobs Act Provisions

Business Interest Deduction Limitation

Summary: Under TCJA, beginning in the 2018 tax year the net interest expenses (interest expenses less interest earned) of businesses not meeting the gross receipts test was limited to 30% of adjusted taxable income.

Threshold: The gross receipts test stipulates that taxpayers with average gross receipts of less than $25 million in the previous three years are not subject to the business interest deduction limitation. The threshold of $25 million applies in 2018, and will be adjusted for inflation thereafter.

Pre-2017 Law: Prior to TCJA, business interest was limited to 50% for firms with a debt-equity ratio greater than 1.5.

JCT Estimated Budget Impact:

FY 2018	FY 2019	FY 2018-27
+$8.4 billion	+$17.7 billion	+$253.4 billion

Characterization of provision: Decrease in Total Deductions.

Modifications to Net Operating Loss (NOL) Deductions

Summary: Under TCJA NOLs carrybacks are no longer allowed. NOLs can now be carried forward *indefinitely*.

Pre-2017 Law: Prior to TCJA, NOLs were carried back to the two tax years prior to the year in which the NOLs were accrued. Any unapplied NOLs were carried forward for *up to 20 years*.

JCT Estimated Budget Impact:

FY 2018	FY 2019	FY 2018-27
+$6.4 billion	+$10.0 billion	+$201.1 billion

Characterization of provision: Decrease in NOL Deductions.

Global Intangible Low-Taxed Income

Rationale: With TCJA's shift toward a territorial tax system, a new category of foreign income, Global Intangible Low-Taxed Income (GILTI), was added to corporate taxable income to reduce incentives for corporate taxpayers to shift profits to low-tax jurisdictions.

Summary: While regular income earned outside the US is not subject to US taxation, any returns earned by a multinational taxpayer in excess of a 10% return on depreciable tangible property in a foreign country that is

subject to less than a 13.125% tax in the foreign territory is considered GILTI. The taxpayer will owe US taxes on GILTI such that the overall rate paid on that income (including US and foreign taxes) is 13.125%.

Tax Rate Schedule: Technically the tax rate on GILTI income in 2018-25 is the standard rate of 21%. However, taxpayers can deduct 50% of GILTI income, reducing the effective rate to as low as 10.5%. In addition, taxpayers receive an 80% foreign tax credit, which means that foreign income taxed at greater than 13.125% is not subject to tax under the GILTI provisions. In 2026, the GILTI deduction will fall from 50% to 37.5%, making the effective tax rate at that time 13.125%.

JCT Estimated Budget Impact:

FY 2018	FY 2019	FY 2018-27
+$7.7 billion	+$12.5 billion	+$112.4 billion

Characterization of provision: Increase in Total Income.

Modelling Notes: The enactment of GILTI will result in some additional foreign tax credits claimed. However, since GILTI provisions only apply on foreign income with tax rates of less than 13.125%, the corresponding increase in foreign tax credits will be small.

Deduction for Foreign Derived Intangible Income

Rationale: While GILTI provisions are the "stick" to discourage multinational taxpayers from shifting intangible income to foreign low-tax jurisdictions, Foreign Derived Intangible Income (FDII) is the "carrot" to attract intangible income to the US

Summary: If a US multinational taxpayer earns a return on depreciable assets of greater than 10%, then the portion of that "excess return" that is allocable to foreign sales is subject to a reduced tax that is lower than the regular corporate tax rate of 21%. The global intangible income (or excess return) is determined first, and then multiplied by the ratio of foreign sales to total sales to determine FDII.

Tax Rate Schedule: The applicable tax rate schedule for FDII is as follows:

- ***2018-2025***: 13.125%
- ***2026-***: 16.83%

JCT Estimated Budget Impact:

FY 2018	FY 2019	FY 2018-27
-$0.2 billion	+$4.8 billion	*-$63.8 billion*

Characterization of provision: Increase in Special Deduction.

Repeal of Corporate Alternative Minimum Tax

Summary: TCJA repealed the Corporate Alternative Minimum Tax (AMT), which was in effect through 2017.

Pre-2017 Law: Prior to TCJA, the AMT was a secondary tax that ran in parallel to the rest of the federal corporate income tax system. The AMT tax rate was lower than the standard corporate income tax rate of 35%, but the AMT calculation did not allow all of the same credits and preferences of the standard corporate income tax calculation. If the taxpayer's liability under the AMT calculation exceeded the taxpayer's regular tax liability (excluding AMT), then the additional AMT was added to the taxpayer's tax liability.

JCT Estimated Budget Impact:[30]

FY 2018	FY 2019	FY 2018-27
-$4.6 billion	*-$4.6 billion*	*-$30.3 billion*

Characterization of provision: Increase in Special Deduction.

[30] Removed effects of budget outlays.