

SUMMARY OF PROPOSAL #22
for consideration by the
ARKANSAS TAX REFORM AND RELIEF LEGISLATIVE TASK FORCE

TOPIC: To Adopt the Depreciation Schedules and Bonus Depreciation as Amended by the Tax Cuts and Jobs Act

Summary of Proposal for Consideration

To adopt the depreciation schedules and bonus depreciation as amended by the Tax Cuts and Jobs Act (TCJA), P.L. 115-97, effective for tax years beginning January 1, 2019.

Fiscal Analysis

According to the Department of Finance and Administration, the revenue loss of adopting both bonus depreciation under 26 U.S.C § 168(k) and depreciation under 26 U.S.C § 179, as amended by the TCJA, beginning in 2019 and after would be as follows: \$137,721,870 loss for FY2020; \$130,121,665 loss for FY2021; \$86,821,197 loss for FY2022; \$53,088,613 loss for FY2023; and \$42,506,460 loss for FY2024.

Legal Analysis

Background

Arkansas Code § 26-51-428 adopts 26 U.S.C § 179, as in effect on January 1, 2009, which allows taxpayers to deduct a certain dollar amount of depreciable property in the year purchased rather than capitalizing and depreciating the property. Arkansas allows for 26 U.S.C § 179 depreciation deductions of assets up to \$25,000 with a phase out beginning at \$200,000. Arkansas has not adopted federal bonus depreciation under 26 U.S.C § 168(k), which allows a business to take an immediate first-year deduction on the purchase of eligible business property, in addition to other depreciation.

ACT 118 of 1929 created the Income Tax Act of 1929 and established the first definitions of depreciation and expensing for the purposes of Arkansas income tax, allowing for “[a] reasonable allowance for the depreciation and obsolescence of property used in the trade or business.” The method used to calculate reasonable allowance was set by the Commissioner of Revenue.

ACT 156 of 1957 amended the method by which depreciation and expensing was calculated. For years after 1953, the term “reasonable allowance” was defined to include an allowance computed in accordance with the regulations prescribed by the Commissioner of Revenue under one of four methods:

- (1) The straight line method;
- (2) The declining balance method, using a rate not exceeding twice the rate that would have been used had the annual allowance been computed under the straight line method;
- (3) The sum of the years-digits method; or

- (4) Any other method productive of an annual allowance that, when added to all allowances for the period commencing with the taxpayer's use of the property and including the taxable year, does not during the first two-thirds (2/3) of the useful life of the property exceed the total of the allowances that would have been used had the allowances been computed under the declining balance method.

ACT 382 of 1987 repealed the earlier depreciation provisions and adopted 26 U.S.C § 179, as in effect on January 1, 1987. This act also stipulated that depreciation was to be calculated in accordance with depreciation claimed for federal income tax purposes by allowing twenty-five percent (25%) of the difference resulting from the depreciation adjustment to be taken as income or allowed as a deduction over four (4) years.

ACT 826 of 1989 adopted 26 U.S.C § 179, as in effect on January 1, 1989, which allowed a depreciation deduction up to \$10,000.

ACT 1160 of 1995 adopted 26 U.S.C § 179, as in effect on January 1, 1995, which allowed a depreciation deduction up to \$17,500.

ACT 951 of 1997 adopted 26 U.S.C § 179, as in effect on January 1, 1997, which allowed a depreciation deduction up to \$20,000.

ACT 1129 of 1999 adopted 26 U.S.C § 179, as in effect on January 1, 1999, which allowed a depreciation deduction up to \$25,000.

ACT 218 of 2007 and ACT 613 of 2007 adopted 26 U.S.C § 179, as in effect on January 1, 2007, which allowed a depreciation deduction up to \$25,000 with a phase out beginning at \$200,000. Arkansas has not adopted any federal changes to 26 U.S.C § 179 since 2007. Arkansas has never adopted bonus depreciation under 26 U.S.C. § 168(k).

Under the TCJA, 26 U.S.C § 179 has been amended to provide for a depreciation deduction up to \$1,000,000 with a phase out beginning at \$2,500,000. The TCJA also amended 26 U.S.C. § 168(k) to allow for bonus depreciation up to one hundred percent (100%) for assets purchased after September 27, 2017, and before January 1, 2023.

Potential Legal Issues

None.

Other States

- Iowa: Iowa is a static conformity state, which means that the state may adopt federal provisions as of a specific date, and changes in federal law are not automatically incorporated into state law. As of January 1, 2018, Iowa has adopted 26 U.S.C § 179, as amended by the TCJA, subject to the following limitations: \$70,000 for tax year 2018 and \$100,000 for tax years beginning with 2019. However, Iowa has

specifically decoupled from the bonus depreciation provisions under 26 U.S.C. § 168(k). (IA St. § 422.35)

- Louisiana: Louisiana is a rolling conformity state, which means that when federal law provisions are adopted by the state, any changes in federal law are automatically incorporated into state law. Louisiana has not specifically decoupled from federal depreciation and bonus depreciation provisions, and unless it decides to do so, Louisiana will automatically conform to the depreciation schedules under 26 U.S.C § 179, as amended by the TCJA, and bonus depreciation under 26 U.S.C § 168(k), as amended by the TCJA. (IA St. § 47:287.63)
- Mississippi: Mississippi is a non-conformity state, which means that the state adopts only selective parts of federal tax law; any future changes in federal law, even for the parts selectively adopted, are not automatically incorporated into state law. Mississippi has adopted federal depreciation law under 26 U.S.C. § 179. Mississippi has never adopted the federal treatment of bonus depreciation under 26 U.S.C § 168(k). It is unclear whether Mississippi intends to adopt the changes to the depreciations provisions under 26 U.S.C. § 179, but the language of Mississippi's law does not explicitly limit the adoption of this provision to a certain date. (MS St. § 27-7-17; Miss. Admin. Code 35-III-5.04)
- Missouri: Missouri is a rolling conformity state, which means that when federal law provisions are adopted by the state, any changes in federal law are automatically incorporated into state law. Missouri has adopted the federal depreciation law under 26 U.S.C. § 179 and the bonus depreciation provisions of 26 U.S.C. § 168(k), subject to limitations for the changes made in 2002 for certain property, and unless Missouri decouples from these provisions, it will automatically conform to the depreciation schedules under 26 U.S.C § 179, as amended by the TCJA, and bonus depreciation under 26 U.S.C § 168(k), as amended by the TCJA. (MO St. § 143.121)
- Oklahoma: Oklahoma is a rolling conformity state, which means that when federal law provisions are adopted by the state, any changes in federal law are automatically incorporated into state law. Oklahoma has adopted the federal depreciation law under 26 U.S.C. § 179 and the bonus depreciation provisions of 26 U.S.C. §168(k). However, for assets placed into service during the 2008 and 2009 tax years, bonus depreciation is limited in that the taxpayer's income is increased by 80% of the bonus depreciation amount allowed under federal law, and the taxpayer may subtract 25% of the amount added back in each of the next three (3) tax years. Unless Oklahoma decouples from these provisions, it will automatically conform to the depreciation schedules under 26 U.S.C § 179, as amended by the TCJA, and bonus depreciation under 26 U.S.C § 168(k), as amended by the TCJA. (68 OK St. §§ 2358 and 2358.6)
- Tennessee: Tennessee is a rolling conformity state, which means that when federal law provisions are adopted by the state, any changes in federal law are

automatically incorporated into state law. Tennessee has adopted the depreciation provisions of federal law, and unless it decouples from this provision, it will automatically conform to the depreciation schedules under 26 U.S.C § 179, as amended by the TCJA. Tennessee has specifically decoupled from bonus depreciation under 26 U.S.C § 168(k). (TN St. § 67-4-2006)

- Texas: Texas is a static conformity state, which means that the state may adopt federal provisions as of a specific date, and changes in federal law are not automatically incorporated into state law. Texas has adopted 26 U.S.C § 179, as in effect on January 1, 2017, and allows depreciation up to a \$25,000 maximum deduction with a \$200,000 investment limit. Texas has not adopted bonus depreciation under 26 U.S.C § 168(k). (TX St. §§ 171.0001 and 171.1011)