State of Arkansas
Department of Finance and Administration
Fiscal Impact Statement

Bill: HB1910
Bill Subtitle: TO ALLOW A DEDUCTION FOR CERTAIN QUALIFIED BUSINESS EXPENSES UNDER THE INCOME TAX ACT OF 1929.

Sponsor:

Rep. Lundstrum

Basic Change:

HB1910 adopts the provisions of 26 U.S.C. § 199A(a)-(h) as in effect on January 1, 2025. These are commonly referred to as the "qualified business income" (QBI) deductions. The federal provisions provide for a 20% deduction for qualified business income by a pass-through entity which HB1910 would adopt for Arkansas income tax purposes.

Specifically, 26 U.S.C. § 199A provides a 20% deduction for the income, deduction, loss, and gain from a pass-through business for items connected with that business conducted in the United States or Puerto Rico. Specifically excluded from the QBI calculations are:

- Wage income;
- Reasonable compensation to an S corporation shareholder for services provided to the S corporation;
- Guaranteed payments to a partner for services provided to a partnership; and
- Investment income unrelated to a trade or business as defined in the Internal Revenue Code.

Currently, the provisions of 26 U.S.C. § 199A are set to expire December 31, 2025. HB1910 does not adopt the federal language providing an expiration date.

HB1910 is effective for tax years beginning on or after January 1, 2025.

Fiscal Impact:

FY2026 - $108M General Revenue Reduction

Taxpayer Impact:

The bill will allow taxpayers to claim a deduction for certain qualified business expenses, aligning with federal law under 26 U.S.C. § 199A(a)-(h).

Resources Required:

The Arkansas Integrated Revenue System (AIRS) will require programming at an estimated cost of $16,000 with no annual maintenance. Tax forms and instructions will need to be updated.

Time Required:

Adequate time is provided for implementation.

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Procedural Changes:

Department employees will need to be educated as well as the tax community.

Other Comments:

Introduced by the Tax Cuts and Jobs Act of 2017 (TCJA), Section 199A aims to provide tax relief to owners of pass-through businesses (sole proprietorships, partnerships, S corporations) and some trusts and estates. It allows eligible taxpayers to deduct up to 20% of their Qualified Business Income (QBI), plus 20% of qualified Real Estate Investment Trust (REIT) dividends and qualified Publicly Traded Partnership (PTP) income.

The deduction is available regardless of whether taxpayers itemize deductions on Schedule A or take the standard deduction. Eligible taxpayers can claim the deduction for tax years beginning after December 31, 2017, and ending on or before December 31, 2025.

Under current law, Section 199A is temporary and scheduled to expire after December 31, 2025. Unless extended by Congress, it will not apply to tax years beginning in 2026 or later. The bill does not have a similar sunset provision so it would continue in Arkansas even if the Federal deduction is allowed to expire.

Congress made numerous changes to the taxation of individuals and corporate and noncorporate businesses as part of P.L. 115-97 (commonly known as the Tax Cuts and Jobs Act or TCJA). Among those changes was a permanent cut in the corporate income tax rate from a top rate of 35% in a graduated rate structure to a single rate of 21%. During the congressional debate over the TCJA, pass-through business owners sought tax relief comparable to any reduction in corporate tax rates. To accommodate the owners, Congress added a new deduction for pass-through business under Internal Revenue Code (IRC) Section 199A and slightly reduced individual income tax rates.

Arkansas has lowered the corporation tax rate in recent years, but it still exceeds the top income tax rate for individual income taxpayers unlike the federal tax rates. This may provide an incentive for some small corporations to convert to eligible pass-through entities to take advantage of the additional tax deduction.

Legal Analysis:

None.