State Compliance with the Job Creation and Worker Assistance Act of 2002

PRESIDENT GEORGE W. BUSH SIGNED THE Job Creation and Worker Assistance Act (JCWAA) of 2002 (Pub L 107-147) on March 9, 2002. This bill provides tax incentives for economic stimulus for both businesses and individual taxpayers. The two major areas immediately affecting businesses are "bonus" depreciation and an extension of Net Operating Loss (NOL) carryback. As a result of the signing of this federal bill, each state requiring income tax has had to consider the potential consequences of these tax provisions for state income taxes to its taxable revenue. Not surprisingly, some states have adopted both, one, or neither of these two changes, and some states have adopted special treatment of these issues. This article provides a capsule view of the states' reactions as of November 20, 2002, to be used as a reference when filing state returns or when determining whether or not to file amended state returns. Please note that state laws change frequently and should be consulted before the actual filing of any state returns.

The "bonus" depreciation is an extra 30% depreciation that may be taken for qualified property purchased after September 10, 2001, and before September 11, 2004. The NOL carryback extends the carryback from two years to five years for tax years ending after December 31, 2000, and before January 1, 2003. Both tax provisions are retroactive to year 2001. The details of the "bonus" depreciation and the NOL carryback are not covered in this article since they have been covered in earlier tax columns (see Stewart S. Karlinsky, May 2002, and L. Stephen Cash and Thomas L. Dickens, August and September 2002).

Because these federal tax incentives come at a time when most states' budgets are being cut, the majority of states are reluctant to accept the "bonus" depreciation and extended NOL provisions, which would decrease their tax revenue. In fact, an overview of state compliance with this legislation shows that the majority do not follow either provision and that only two states, Alaska and North Dakota, adopt both.

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Bonus Depreciation

Of the two tax incentives, "bonus" depreciation is more widely accepted. Thirteen states comply with the federal "bonus" depreciation, either because state laws require automatic conformity with federal treatments of depreciation or via state legislation. Twenty-two states and the District of Columbia rejected the "bonus" depreciation: Arizona, Arkansas, California, Connecticut, Georgia, Hawaii, Idaho, Indiana, Iowa, Kentucky, Maryland, Massachusetts, Michigan, Mississippi, New Hampshire, New Jersey, Rhode Island, South Carolina, Tennessee, Vermont, Virginia, and Wisconsin. And the following 11 states adopted a special version of it:

Illinois: The "bonus" depreciation must be added back to taxable income, but the regular federal depreciation rules still apply. Income tax filers should use the specially formatted IL-4562 form, which is especially helpful to taxpayers when assets have been disposed or sold.

Maine: The state allows "bonus" depreciation through 2001, but any claims in 2002, 2003, and 2004 are to be added back. The amount added back can then be subtracted evenly over three years, starting two years after the date of the add-back.

Minnesota: 80% of the "bonus" depreciation is added back to taxable income in the first tax year ending after September 10, 2001. The amount added back can then be subtracted in even amounts over the next five years.

Missouri: "Bonus" depreciation cannot be applied to purchases made after July 1, 2002, and before June 30, 2003. It may, however, be applied to purchases during any other period between September 11, 2001, and September 10, 2004.

Montana: The actual state reaction is unclear. It is assumed that "bonus" depreciation will be allowed, due to the history of state reactions to federal depreciation guidelines, but no action has been made by the state to accept or reject the measure.

Nebraska: 85% of the "bonus" depreciation is to be added back to taxable income. If the taxpayer is filing a unitary return both in and out of the state, the full amount of "bonus" depreciation must be added back. Any amount added back is to be fully deducted, 20% each year over a five-year period starting in the first taxable year beginning on or after January 1, 2005.

North Carolina: For the 2001 tax year, North Carolina complied with the federal changes. In the 2002 tax year, taxpayers are required to add back all of the "bonus" depreciation, and in 2003 an add-back of 70% of the "bonus" depreciation is required. The amounts added back may then be subtracted evenly over a five-year period starting on or after January 1, 2005.

Ohio: Five-sixths of the "bonus" depreciation is added back to taxable income in the first year. The amount of the add-back may then be evenly subtracted from taxable income over the next five years. For tax years ending before June 5, 2002, the add-back must be elected in order to take the "bonus" depreciation in that year or any subsequent year.

Oklahoma: 80% of "bonus" depreciation is added back to taxable income in the first year. This amount is then evenly subtracted from taxable income over the next four years.

Pennsylvania: Three-sevenths of the "bonus" depreciation is allowed in the first year. The remaining four-sevenths is added back to taxable income, and an additional depreciation subtraction is made for this portion of the "bonus" using standard depreciation rules.

Texas: The state does not impose an income tax, but "bonus" depreciation is not used to determine regular franchise tax. Alternately, taxpayers qualifying and choosing to file using the Federal Income Tax (FIT) method can use the "bonus" depreciation if they originally used it in determining FIT.

Nevada, South Dakota, Washington, and Wyoming: These states do not impose an income tax, so there is no depreciation expense.

NOL Carryback

With respect to the extension of the NOL carryback to five years, only Alaska, North Dakota, and Vermont allow taxpayers to fully utilize the extension for state tax purposes. Thirty-nine states and the District of Columbia either did not adopt the new federal NOL carryback treatment or have separate state provisions dealing with NOL carryback. Three states limit the NOL carryback amounts ($30,000 in Delaware, $10,000 in New York, and $300,000 in West Virginia), while one state, Oklahoma, limits the NOL carryback to losses incurred during tax years beginning on or after January 1, 2001. Losses incurred before that date cannot be carried back. Finally, Nevada, South Dakota, Washington and Wyoming do not impose an income tax, so there is no NOL carryback.

Tax Incentives

The enactment of JCWAA in 2002 is intended to provide an avenue for economic stimulus by granting business tax incentives of 30% "bonus" depreciation and an extension of NOL carryback from two to five years. But most states, if they were to adopt these provisions, would lose a great deal of tax revenue during a period when their resources are already stretched. As a result, the majority of the states have rejected one or both measures. ■

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