



B-25/05  
June 7, 2005

## **Most States Will Conform to Sec. 199 Qualified Production Activity Income Deduction**

### *Results of Survey of Tax Administrators*

#### **Summary**

The American Jobs Creation Act (P.L. 108-357) created a new deduction for a specified portion of “Qualified Production Activity Income” (QPAI). Since the QPAI deduction reduces federal taxable income, it is a conformity issue for states, since nearly every state begins their corporation income tax with federal taxable income as a starting point. Twenty-seven states will (or are considered likely to) conform to the Sec. 199 QPAI deduction, according to a survey of state tax administrators conducted by the Federation of Tax Administrators in May 2005. Nineteen states have made a determination not to conform to the deduction. (or are considered likely to make such a decision.)

The American Jobs Creation Act (P.L. 108-357) created a new deduction for a specified portion of “Qualified Production Activity Income” (QPAI). The deduction is codified at section 199 of the Internal Revenue Code. Generally, speaking QPAI is net income from domestic (U.S.) operations in a range of manufacturing, extraction, processing and related activities. The deduction starts at 3 percent of QPAI in 2005 and increases to 9 percent in tax year 2010.

Since the QPAI deduction reduces federal taxable income, it becomes an issue of conformity for states since nearly every state begins their corporation income tax with federal taxable income as a starting point.<sup>1</sup> States have dealt with this issue during the 2005 legislative sessions.

The attached map shows the results of a survey of state tax agencies regarding their conformity to the Section 199 QPAI deduction for tax year 2005. In the map, where the term “Likely” is used to characterize a state, the legislature is still in session and the issue has not been finally disposed of. The characterization is intended to provide the best assessment of the current situation. As shown, 27 states will (or are considered likely to) conform to the Sec. 199 QPAI deduction. Nineteen states have made a determination not to conform to the deduction (or are considered likely to make such a decision.)

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<sup>1</sup> The QPAI deduction is also available on individual returns and for shareholders or other recipients of pass-through entity income. This survey focuses only on corporation income taxes.

Also attached is a spreadsheet that displays the same results. It also contains an entry indicating whether the state's conformity to the federal Internal Revenue Code for corporate income tax purposes is "fixed" as of a particular date and requires legislative action to update it or whether it is "automatic," meaning it is to the IRC for the tax year in question without the need for legislative action.

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## State Conformity to IRC Sec. 199 QPAI Deduction

June 1, 2005

State Name	Type of Conformity	Conform to Sec. 199	State Name	Type of Conformity	Conform to Sec. 199
Alabama	Automatic*	Yes	Missouri	Automatic	Yes
Alaska	Automatic	Likely Yes	Montana	Automatic	Yes
Arizona	Fixed	Yes	Nebraska	Fixed	Likely Yes
Arkansas	Fixed	No	Nevada	N/A	N/A
California	Fixed	Likely Not	New Hampshire	Fixed	Likely Not
Colorado	Automatic	Yes	New Jersey	No IRC Reference	Likely Not
Connecticut	Automatic	Yes	New Mexico	Automatic	Yes
Delaware	Automatic	Likely Yes	New York	Automatic	Likely Yes
District of Columbia	Fixed	No	North Carolina	Fixed	No
Florida	Fixed	Yes	North Dakota	Automatic	No
Georgia	Fixed	No	Ohio	Fixed	Yes
Hawaii	Fixed	No	Oklahoma	Automatic	Yes
Idaho	Fixed	Yes	Oregon	Fixed	Likely Yes
Illinois	Automatic	Likely Yes	Pennsylvania	Automatic*	Likely Yes
Indiana	Fixed	No	Rhode Island	Fixed	Likely Not
Iowa	Fixed	Yes	South Carolina	Fixed	Likely Not
Kansas	Automatic	Yes	South Dakota	N/A	N/A
Kentucky	Fixed	Yes	Tennessee	Automatic	No
Louisiana	Automatic	Likely Yes	Texas	Fixed	No
Maine	Fixed	No	Utah	Automatic	Yes
Maryland	Automatic	No	Vermont	Fixed	Likely Yes
Massachusetts	Automatic	No	Virginia	Fixed	Yes
Michigan	See Note	Likely Yes	Washington	N/A	N/A
Minnesota	Fixed	Likely Not	West Virginia	Fixed	No
Mississippi	No IRC Reference	No	Wisconsin	Fixed	Likely Yes
			Wyoming	N/A	N/A

\*Alabama - Conform on Corporate Tax Only. Regular session has adjourned.

\*Michigan - Reference is the IRC as of 1/1/99, but the IRC in effect for the tax year may be used at the option of the taxpayer.

\*Pennsylvania - Conform on corporate net income tax only.

Source: Federation of Tax Administrators based on survey responses from state tax agencies.