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State Tax Changes Effective January 1, 2022

Timothy Vermeer Senior Policy Analyst
Savanna Funkhouser Research Associate

Key Findings

- Twenty-one states and the District of Columbia had significant tax changes take effect on January 1, 2022
- Five states (Arizona, Arkansas, Louisiana, North Carolina, and Oklahoma) cut individual income taxes effective January 1. The District of Columbia was the only jurisdiction to increase income taxes.
- Four states (Arkansas, Louisiana, Nebraska, and Oklahoma) saw corporate income tax rates decrease. Florida is the only state to increase corporate income tax rates, as a temporary reduction expired.
- Five states (Arizona, Colorado, Georgia, Illinois, and Oregon) implemented a pass-through entity election to serve as a workaround to the federal state and local tax (SALT) deduction cap.
- Iowa is phasing out its inheritance tax, while Maryland and Washington face litigation over new taxes on digital advertising and capital gains income respectively.

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Editor, Rachel Shuster
Designer, Dan Carvajal

Tax Foundation
1325 G Street, NW, Suite 950
Washington, DC 20005

202.464.6200

taxfoundation.org

Introduction

States, as Justice Louis Brandeis once wrote, are the laboratories of democracy,¹ and those laboratories have been remarkably busy in recent years as, 90 years since Justice Brandeis coined the phrase, states continue to produce unique responses to policy challenges and opportunities.

As the nation enters 2022, 21 states and the District of Columbia have significant tax changes taking effect. Some states have chosen to respond to budget surpluses associated with the pandemic recovery by enacting individual and corporate income tax (CIT) cuts. Other states, uncertain as to the impact of the pandemic on state revenue, opted to raise taxes. Some states will implement tax changes adopted by elected representatives while others will implement changes adopted through ballot measures.

Among the more novel tax policy “experiments” to be implemented in 2022 is Maryland’s first-in-the-nation digital advertising tax. Meanwhile, five new states will join the list of those that allow pass-through businesses to be taxed at the entity level to sidestep federal limits on state and local tax (SALT) deductions. And Washington is attempting to implement a 7 percent capital gains tax under a constitution which defines income as a form of property and allows no property to be taxed at a rate greater than 1 percent.

All 22 jurisdictions with significant changes are highlighted below.

In addition to the tax changes mentioned here, many states will see automatic adjustments to a range of tax rates, from inflation-indexing of gas taxes or income tax rates and brackets to formula-driven adjustments to unemployment insurance tax rates. Some revisions adopted in 2021 legislative sessions will start at a later date (often July 1st, the beginning of the fiscal year in most states), while a substantial increase in New York’s individual and CIT rates was implemented retroactive to 2021.²

Arizona

Arizona’s 2022 tax changes are among the nation’s most complex, as they involve—among other things—the unwinding of a prior ballot measure. Proposition 208 (2020) had created a 3.5 percent high earners tax atop the state’s existing 4.5 percent top marginal income tax rate, functionally yielding a new top rate of 8 percent, with the additional proceeds earmarked for education. Lawmakers effectively undid the ratification through legislation, lowering the base rates to ensure that the combined top rate never exceeded 4.5 percent. They simultaneously adopted revenue triggers that could create a lower, single-rate tax.

Senate Bill 1828 would have started the state’s conversion from a graduated individual income tax to a flat individual income tax on January 1, 2022.³ The transition would have initially collapsed the four current tax brackets into two. Single tax filers with taxable income up to \$27,272 (double if

1 *New State Ice Co. v. Liebmann*, 285 U.S. 262 (1932).

2 As part of the FY 2022 Enacted Budget Bill, New York’s top marginal rate for individual income taxation increased from 8.2 percent to 10.9 percent. Importantly, two tax brackets were added to the individual income tax code. Individuals are now assessed a tax of 9.65 percent on New York taxable income greater than \$1,616,450 but not more than \$5 million. Individuals will be subject to a 10.3 percent tax on taxable income greater than \$5 million but not more than \$25 million. Any taxable income exceeding \$25 million is subject to the top marginal rate of 10.9 percent.

3 S.B. 1828, 55th Leg., First Reg. Sess. (Ariz., 2021), <https://www.azleg.gov/legtext/55leg/1R/bills/SB1828S.pdf>.

filing jointly) would have been taxed at a rate of 2.55 percent. Any taxable income exceeding that amount would have been taxed at a rate of 2.98 percent. Pending revenue triggers, the tax would eventually have been reduced to 2.5 percent, regardless of income level. However, enough signatures were gathered via petition that voters will now be required to approve the flat tax via ballot measure (Proposition 307) in the November 2022 election. In the meantime, implementation of S.B. 1828 has been suspended.

Pending the outcome of Proposition 307, Arizona's top marginal rate will be capped at 4.5 percent, even though a final decision on Proposition 208 is still pending judicial review.⁴ Since the Arizona Supreme Court refused to suspend the law⁵ while a lower court adjudicates details pertaining to the measure's revenue allocation, the surtax remains in effect. Therefore, policymakers enacted S.B. 1827, to counteract the effects of Proposition 208 by automatically reducing the top marginal individual income tax rate by an amount that would keep both the surtax and the top rate combined from exceeding 4.5 percent.

Finally, under provisions of H.B. 2838,⁶ Arizona will allow partnerships, limited liability companies (LLCs), and S corporations to pay a 4.5 percent tax at the entity level instead of having all business-related income pass through to the individual income tax. The law was passed as a SALT deduction cap workaround.⁷

Arkansas

As a part of reforms begun in 2019,⁸ Arkansas's CIT rate decreased from 6.2 percent to 5.9 percent on January 1, 2022. This is the second of two corporate rate reductions legislated under Act 822.

Arkansas's top individual income tax rate will decline from 5.9 percent to 5.5 percent as a result of legislation passed during the state's December 2021 special session.⁹ Arkansas is unique in having three different tax rate schedules depending on income level, and in 2022, the rate of nearly every intermediate tax bracket was also reduced as legislators voted to collapse the two lower tax tables into one.

California

Beginning January 1, 2022, California's cannabis cultivation taxes increased to reflect an adjustment for inflation as required under the Cannabis Tax Law. Flowers are now taxed at a rate of \$10.08 per dry-weight ounce; leaves are taxed at a rate of \$3.00 per dry-weight ounce; and fresh cannabis plants are taxed at \$1.41 per ounce.¹⁰ Prior to the New Year, flowers were taxed at a rate of \$9.65 per dry-weight ounce; leaves at \$2.87 per dry-weight ounce; and fresh cannabis plants at \$1.35 per ounce.¹¹

4 Howard Fischer, "Court Rules Prop 208 Surcharge Can Stay – For Now," *Arizona Capitol Times*, Aug. 19, 2021, <https://www.azcapitoltimes.com/news/2021/08/19/court-rules-prop-208-surcharge-can-stay-for-now/>.

5 *Fann v. Arizona*, 493 P.3d 246 (Ariz., 2021).

6 H.B. 2838, 55th Leg., First Reg. Sess. (Ariz., 2021.) <https://apps.azleg.gov/BillStatus/GetDocumentPdf/490546>.

7 Ibid.

8 2019 Ark. Acts 822 at sec. 4(a)(3).

9 S.B. 1, 93rd Gen. Assy., Second Spec. Sess. (Ark., 2021). <https://www.arkleg.state.ar.us/Bills/FTPDocument?path=%2FBills%2F2021S2%2FPublic%2FSB1.pdf>.

10 See California Department of Tax and Fee Administration, "Tax Guide for Cannabis Businesses," <https://www.cdtfa.ca.gov/industry/cannabis.htm>.

11 Ibid.

Colorado

On June 23, 2021, Governor Jared Polis (D) signed H.B. 1311,¹² adopting the Finnegan Rule for determining which affiliated companies are considered part of a unitary group for corporate income purposes. Colorado is a combined reporting state, which means that the gains and losses of all taxable affiliated companies are combined on a single return, but under the Finnegan Rule, it will no longer be necessary that each entity included in the joint return have its own nexus with the state of Colorado, as was the case under the Joyce Rule.

Another bill, H.B. 1327, establishes an optional entity-level tax regime for pass-through businesses.¹³ The new law allows S corporations, partnerships, and LLCs to elect to be taxed as an entity rather than on the owners' individual income taxes, avoiding the federal cap on SALT deductions. The law is applicable to income tax years beginning on or after January 1, 2022 provided federal SALT deductions are limited in the respective tax year. Income of electing entities would be taxed at 4.55 percent.

District of Columbia

As of January 1, 2022, Washington, D.C.'s individual income tax changed considerably. Enacted via the Fiscal Year 2022 Budget Support Act of 2021, the District increased the number of tax brackets from six to seven and altered many of the thresholds.¹⁴ Changes begin for individuals with a D.C. taxable income between \$250,000 and \$500,000, assessed a tax of \$19,560 plus 9.25 percent of the excess over \$250,000. Those with taxable income over \$500,000 but not over \$1 million will pay \$42,775 plus 9.75 percent of the excess over \$500,000. Finally, individuals with taxable income over \$1 million will be taxed \$91,525 plus 10.75 percent on any amount over \$1 million.

Florida

Florida's CIT rate decreased by nearly 1 percentage point in 2021, but it changed again—at least for a short time—at the beginning of 2022.¹⁵ Florida ended 2021 with the nation's second-lowest CIT rate, at 3.535 percent.¹⁶ Only North Carolina had a lower rate, at 2.50 percent. As of January 1, a key provision of the 2019 tax reform sunsetted, with the CIT snapping back to 5.5 percent.¹⁷ With this reversion, Florida now ranks 11th among states with a CIT, at least until policymakers decide whether to extend the 2021 reduction or to make it permanent.

12 H.B. 21-1311, 73rd Gen. Assy., First Reg. Sess. (Colo., 2021).

13 H.B. 21-1327, 73rd Gen. Assy., First Reg. Sess. (Colo., 2021).

14 See Bill 24-285, "Amendment in the Nature of a Substitute" (D.C., 2021).

15 Timothy Vermeer, "Florida Lawmakers Should Provide Certainty Around the State's Corporate Income Tax Rate Reduction," Tax Foundation, Oct. 1, 2021, <https://www.taxfoundation.org/florida-corporate-income-tax/?web=1&wdLOR=c5DB377B8-0920-46C7-A13B-412F2BFF052A>.

16 Janelle Cammenga, "State Corporate Income Tax Rates and Brackets for 2021," Tax Foundation, Feb. 3, 2021, <https://www.taxfoundation.org/publications/state-corporate-income-tax-rates-and-brackets/>.

17 Fla. Stat. § 220.1105 (2021).

Georgia

As of New Year's Day 2022, partnerships and S corporations in Georgia are allowed to elect whether business income will be as an entity. Pursuant to the passage of H.B. 149,¹⁸ the Georgia taxable income of electing pass-through businesses will be taxed at 5.75 percent. The change effectively isolates small business income and taxes it at the same rate as corporate income, another example of a workaround for the federal SALT deduction cap for pass-through businesses.

Illinois

Under S.B. 2531 signed by Governor J.B. Pritzker (D) on August 27, 2021, Illinois will allow partnerships and S corporations to elect to be taxed as an entity.¹⁹ The election may be made for tax years starting on or after January 1, 2022 and before January 1, 2026. Illinois, in addition to its statutory income tax rate of 4.95 percent, also has a 1.5 percent "personal property replacement tax," an additional income tax that is imposed on pass-through businesses, originally to offset revenue from the repeal of tangible property taxes. This additional tax remains in place.

Iowa

With the passage of S.F. 619, Iowa policymakers set the state on course to eliminate the inheritance tax by the first day of 2025.²⁰ Rates will be phased down in five uniform reductions.²¹ The revisions to the inheritance tax law were enacted June 16, 2021, with the first rate reduction made retroactive to New Year's Day 2021. The second round of reductions went into effect on January 1, 2022, yielding a 40 percent reduction in pre-reform rates. After Iowa's inheritance tax is eliminated, only five states (Kentucky, Maryland, Nebraska, New Jersey, and Pennsylvania)²² will continue to tax beneficiaries on the value of their inherited property.

Kentucky

With the enactment of H.B. 249 over the veto of Governor Andy Beshear (D), Kentucky will make significant changes to its film tax credit.²³ For applications approved on or after January 1, 2022, film companies are now authorized to receive a refundable tax credit. Prior to 2022, companies could receive a credit offsetting Kentucky income or limited liability entity taxes, but they could not claim more subsidy than they owed in taxes. This restores a level of generosity to film tax credits that the Commonwealth had previously curtailed, in line with other states increasingly recognizing the poor return they offer. The total value of all refundable credits now authorized by the Commonwealth is \$75 million.

18 H.B. 149, 156th Gen. Assy., Reg. Sess. (Ga., 2021).

19 S.B. 2531, 102nd Gen. Assy., Reg. Sess. (Ill., 2021).

20 S.F. 619, 89th Gen. Assy., Reg. Sess. (Iowa, 2021).

21 Code of Iowa § 450.10 (2022).

22 Janelle Cammenga, "Does Your State Have an Estate or Inheritance Tax?," Tax Foundation, Feb. 24, 2021, <https://www.taxfoundation.org/state-estate-tax-state-inheritance-tax-2021/>.

23 H.B. 249, 2021 Gen. Assy., Reg. Sess. (Kent., 2021).

Louisiana

With the approval of Amendment No. 2 by the voters on November 13, 2021,²⁴ four significant tax changes took effect in Louisiana on January 1, some resulting directly from the constitutional amendment and others through the implementation of legislation that was contingent on that constitutional ratification. First, the maximum individual income tax rate permitted by the state constitution decreased from 6 percent to 4.75 percent.²⁵ Second, the amendment eliminated the mandatory deduction of federal income taxes from state income taxes.²⁶

Third, as of January 1, 2022, H.B. 278 reduced individual income tax rates from 2 percent, 4 percent, and 6 percent to 1.85 percent, 3.5 percent, and 4.25 percent respectively.²⁷ Finally, H.B. 292 collapsed Louisiana's five CIT rates into three.²⁸ The new system taxes the first \$50,000 of corporate net income at 3.5 percent. The next \$100,000 will be taxed at 5.5 percent, and any income over \$150,000 will be taxed at 7.5 percent. The top marginal rate is reduced by 0.5 percentage points but kicks in at a threshold \$50,000 lower than in 2021. Both H.B. 278 and H.B. 292 were passed during Louisiana's regular 2021 legislative session but enactment was contingent on voters' assent to Amendment No. 2.

Unrelated to the constitutional amendment, Louisiana enacted S.B. 36, which affects the carryforward of net operating losses (NOLs).²⁹ Instead of a 20-year window in which to carry forward all losses from a given year, the state now allows NOLs from tax years beginning January 1, 2001 to be carried forward until exhausted. Such cases are applicable to tax returns filed after January 1, 2022.

Governor John Bel Edwards (D) also signed S.B. 157 on June 16, 2021.³⁰ The law, effective January 1, 2022, responds to an increasingly remote workforce by eliminating the requirement for an employer to withhold income taxes from wages of a nonresident employee if the employee worked in the state for 25 days or fewer during the calendar year. If nonresidents work in Louisiana for more than 25 days, withholding must occur for the entire period the employee operated in the state.

Maryland

Maryland's first-in-the-nation digital advertising tax, enacted initially as part of H.B. 732,³¹ took belated effect on New Year's Day 2022. Passed by overriding the veto of Governor Larry Hogan (R), the law was initially to take effect on March 14, 2021. However, it was delayed in February 2021 by S.B. 787 so policymakers could have time to make additional changes to the law.³² Under the new policy, the first \$100 million in annual global gross receipts generated through online advertising will be exempt from taxation. Receipts between \$100 million and \$1 billion will be subject to a tax of 2.5

24 See Louisiana Secretary of State, "Statement of Proposed Constitutional Amendments October 9, 2021," <https://www.sos.la.gov/ElectionsAndVoting/PublishedDocuments/ProposedConstitutionalAmendments2021Summaries.pdf>.

25 S.B. 159, 2021 Leg., Reg. Sess. (La, 2021).

26 Ibid.

27 H.B. 278, 2021 Leg., Reg. Sess. (La, 2021).

28 H.B. 292, 2021 Leg., Reg. Sess. (La, 2021).

29 S.B. 36, 2021 Leg., Reg. Sess. (La, 2021).

30 S.B. 36, 2021 Leg., Reg. Sess. (La., 2021).

31 H.B. 732, 2020 Gen. Assy., Reg. Sess. (Md., 2020).

32 S.B. 787, 2021 Gen. Assy., Reg. Sess. (Md. 2021).

percent. A 5 percent rate will be assessed on receipts between \$1 billion and \$5 billion; 7.5 percent on \$5 billion to \$15 billion; and 10 percent on gross receipts exceeding \$15 billion. The tax is the subject of pending litigation on its constitutionality and potential conflict with the federal Permanent Internet Tax Freedom Act, most immediately in *U.S. Chamber of Commerce v. Franchot*.

Mississippi

As of January 1, 2022, Mississippi has completed the phaseout of its 3 percent individual and CIT brackets. The state has been slowly eliminating its lowest tax bracket by exempting \$1,000 increments every year since 2018. The Magnolia State now effectively exempts the first \$5,000 of taxable income while assessing a 4 percent tax on the next \$5,000 and a 5 percent tax on all taxable income above \$5,000.

Montana

Montana legalized the sale of recreational marijuana as of January 1, 2022, along with a 20 percent tax on the retail price of marijuana. The legalization and excise tax were approved by 57 percent of voters who weighed in on Initiative No. 190 on the 2020 ballot.³³ Under H.B. 701, which enacted changes to marijuana regulations and taxation, counties also have the option of enacting up to a 3 percent local-option excise tax on the retail value of marijuana sales provided the surtax is approved by voters.³⁴ Medical marijuana will continue to be taxed at 4 percent of its retail value.³⁵

Nebraska

Nebraska began a two-stage reduction to the CIT this year. Under L.B. 432, the top marginal corporate rate (applied to income over \$100,000) was reduced from 7.91 percent to 7.5 percent.³⁶ The lower marginal rate (5.58 percent, applied to the first \$100,000 of income) is unchanged.

New Hampshire

As of New Year's Day 2022, the filing threshold for the business enterprise tax increased. Businesses will be required to file a return if they have gross receipts greater than \$250,000 or an enterprise value tax base greater than \$250,000. The type of return will be a function of the larger of whichever base meets the \$250,000 minimum. The change to the business enterprise tax was enacted as part of the biennial budget, H.B. 2, signed into law by Governor Chris Sununu (R) on June 25, 2021.³⁷

33 See Montana Secretary of State, "2020 General Election—November 3, 2020," <https://electionresults.mt.gov/resultsSW.aspx?type=BQ&map=CTY>, last updated Sept. 10, 2021.

34 H.B. 701, 67th Leg., Reg. Sess. (Mont., 2021).

35 Ibid.

36 L.B. 432, 107th Leg., First Session, (Neb., 2021).

37 H.B. 2, 2021 Gen. Court, Reg. Sess. (N.H., 2021).

North Carolina

Under provisions of North Carolina's biennial budget bill signed by Governor Roy Cooper (D) on November 18, 2021, the state's flat income tax rate was reduced to 4.99 percent on January 1, 2022.³⁸ This is the first of six incremental reductions that will ultimately reduce the rate to 3.99 percent by tax year 2027. The budget bill also provides for the full future phaseout of the CIT.

Oklahoma

Oklahoma implemented numerous changes to the individual income tax in addition to two business-related income tax reductions. H.B. 2962 implemented an across-the-board rate reduction of 0.25 percent.³⁹ The top rate declined from 5 to 4.75 percent, making it the ninth lowest top marginal rate among states that levy an individual income tax. H.B. 2962 also restored the refundability of the state's earned income tax credit (EITC), which was made nonrefundable in 2016.

Lawmakers also approved H.B. 2960, which lowers the CIT from 6 percent to 4 percent,⁴⁰ leaving Oklahoma tied with Missouri for the second-lowest CIT rate in the nation, after North Carolina (2.5 percent). H.B. 2963 applies the same rate to pass-through businesses.⁴¹

Oregon

With the implementation of S.B. 727 on January 1, 2022,⁴² Oregon joined a growing list of states that have legislated SALT deduction workarounds on behalf of pass-through business owners. Oregon's pass-through business alternative income tax is similar to other states' in that it allows S corporations, LLCs, and partnerships to isolate business income for tax purposes. Electing entities would be subject to a 9 percent tax on taxable income up to \$250,000 and 9.9 percent tax on taxable income exceeding that amount. If a business owner or partnership elects to forgo the election, taxable income in excess of \$125,000 for a single filer would be subject to the top marginal rate of 9.9 percent. This alternative tax regime is currently available through the end of 2024.

Washington

Washington implemented a 7 percent tax on long-term net capital gains in excess of \$250,000 beginning January 1, 2022. Real estate, retirement savings accounts, livestock, and timber are exempt from taxation. On November 2, 2021, the law was the subject of a non-binding advisory vote where 61 percent of voters expressed their desire to repeal the tax. While the law took effect at the start of the new year, it will also wind its way through the courts. Litigation is currently pending, since the state's constitution restricts income taxation, with proponents of the new tax arguing that it is not a tax on income but rather an excise tax denominated in net income.

38 S.B. 105, 2021 Gen. Assy., Reg. Sess. (N.C., 2021).

39 H.B. 2962, 2021 Leg., Reg. Sess. (Okla., 2021).

40 H.B. 2960, 2021 Leg., Reg. Sess. (Okla., 2021).

41 H.B. 2963, 2021 Leg., Reg. Sess. (Okla., 2021).

42 S.B. 727, 81st Legislative Assy., Reg. Sess. (Ore., 2021).

West Virginia

Since enactment of H.B. 2001 in 2019, West Virginia has been phasing in an income tax exemption for Social Security benefits.⁴³ Thirty-five percent of benefits were exempt from taxation in tax year 2020; 65 percent of benefits were exempt in 2021; and 100 percent of benefits are exempt as of January 1, 2022. The exemption is means-tested, so some taxpayers will not qualify. Joint tax filers with a federal adjusted gross income of more than \$100,000 or single filers with a federal adjusted gross income of more than \$50,000 will be excluded.

Wyoming

On February 9, 2021, Governor Mark Gordon (R) signed S.F. 60 into law,⁴⁴ which, as of January 1, 2022, requires Wyoming mining companies to remit *ad valorem* taxes on production to county governments on a monthly basis. Prior to the law's implementation, companies were required to pay *ad valorem* taxes semiannually. However, remittance often lagged production by up to 18 months. In certain instances, mining firms would go bankrupt before local governments received the overdue revenue. The payment schedule was changed to mitigate the fiscal impact on county governments.

43 H.B. 2001, 2019 Reg. Sess. (W. Va., 2019).

44 S.F. 60, 66th Leg., Gen. Sess. (Wyo., 2021).