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UPDATED: Massachusetts Legislature Passes Wide-Ranging Tax Bill Impacting Estate and Income Taxes

Update (10/04/2023): Governor Maura Healey signed this legislation into law on Wednesday, October 4. In a significant move, the Massachusetts Legislature has voted to pass a sweeping $1 billion tax package that will modify a wide range of Massachusetts tax laws, including those related to the estate tax, the recently enacted "millionaires' tax" and the short-term capital gains rate. The bill now moves to Governor Maura Healey for approval, which could result in additional changes. The Massachusetts estate tax, in its current form, applies to any person who dies with assets in excess of $1 million. The entire estate, not just the amount in excess of $1 million, is subject to estate tax. The newly passed bill increases the threshold amount to $2 million, meaning no estates under $2 million will be subject to estate tax. In addition, the bill provides that only assets in excess of $2 million will be subject to the tax. These changes are effective for the estates of individuals dying on or after January 1, 2023. The bill brings some clarity to the millionaires' tax, which, as previously reported, is a 4 percent surtax on annual taxable income in excess of $1 million that became law on January 1, 2023. Included in the bill is a provision requiring a married couple to file a joint Massachusetts return for any year in which the couple files a joint federal income tax return. This new rule is seemingly designed to dissuade married couples from filing separate Massachusetts tax returns to avoid or minimize the imposition of the millionaires' tax. Notably, this new rule applies to the 2024 tax year, which presumably means married couples can still file a joint federal return and separate Massachusetts returns for the current 2023 tax year. Regarding capital gains taxes, the bill cuts the tax rate for short-term capital gains, which are gains realized from the sale of capital assets held for one year or less, from 12 percent to 8.5 percent. This change is effective for taxable years beginning on or after January 1, 2023. The long-term capital gains rate remains unchanged at 5 percent. In addition to the foregoing, the bill:

- Overhauls how Massachusetts calculates taxes owed by corporations doing business in multiple states, now focusing solely on the company's sales. Under this "single sales factor formula," the amount of a multistate corporation's income that is subject to Massachusetts tax will be determined by the revenue from sales that the corporation conducts in Massachusetts. This new system will replace the current apportionment system, which in addition to sales also takes into account employees and property located within the Commonwealth.
- Increases the tax credit for children, disabled adults or seniors from $180 to $310 in 2023 and then to $440 in 2024.
- Increases the maximum "senior circuit-breaker credit" from $1,200 to $2,400. This is a refundable credit for senior citizens based on real estate taxes or rent paid on residential property owned or rented as a principal residence.
- Increases the cap on the rental deduction from $3,000 to $4,000.
- Increases the Earned Income Tax Credit from 30 percent to 40 percent of the federal credit.
- Increases the maximum credit for homeowners doing septic tank replacement or repair to $18,000.

Notably, the bill also states that the Massachusetts Department of Revenue will analyze the potential impact of implementing an additional, elective entity-level tax of up to 4 percent on qualified taxable income of eligible pass-through entities. Massachusetts is one of many states that have recently enacted "pass-through entity tax" rules to provide relief to taxpayers who can no longer deduct state taxes on their federal tax returns due to the $10,000 "SALT cap" limitation set forth by the Tax Cuts and Jobs Act in 2017. The current pass-through entity tax rules in Massachusetts assume a 5 percent tax rate and fail to take into account the additional 4 percent surtax imposed by the millionaires' tax. The Department of Revenue has now indicated that it will consider whether to expand the pass-through entity tax rules to also help taxpayers achieve the economic effect of a federal tax deduction for millionaires' tax paid, but as of now that benefit is not available.

Authors

Christine N. Fletcher
Partner

Boston, MA | (617) 345-4686

cfletcher@daypitney.com

Justin M. Hannan
Partner

Boston, MA | (617) 345-4619

jhannan@daypitney.com

Christopher A. Voukides
Partner

Boston, MA | (617) 345-4627

cvoukides@daypitney.com

David S. Raymon
Partner

Boston, MA | (617) 345-4689

draymon@daypitney.com

David L. Silvian
Partner

Boston, MA | (617) 345-4655

dsilvian@daypitney.com

Tiffany M. Bentley
Partner

Boston, MA | (617) 345-4692

tbentley@daypitney.com

Ann Hetherwick Cahill
Partner

Boston, MA | (617) 345-4691

hcahill@daypitney.com

Meredith H. Greene
Partner

Boston, MA | (617) 345-4622

mgreene@daypitney.com

Amy R. Lonergan
Partner

Boston, MA | (617) 345-4613

alonergan@daypitney.com

Leiha Macauley
Partner

Boston, MA | (617) 345-4602

lmacauley@daypitney.com

Jordana G. Schreiber
Partner

Boston, MA | (617) 345-4608

jschreiber@daypitney.com