

The Bankler Report

January 4, 2018

INTRODUCTION

On December 22, President Trump signed Tax Cuts and Jobs Act (Public Law 115-97) into law. This report deals primarily with business provisions. Except for changes in depreciation, which were effective on September 27, 2017, most other provisions are effective for tax years beginning after December 31, 2017.

Business Provisions:

- 1. Flat Corporate Tax Rate** -The law replaces the current four-tier schedule of corporate rates (15%, 25%, 34%, and 35%, with a \$75,001 threshold for the 34% rate) with a flat 21% rate (including personal services corporations) effective for years beginning after December 31, 2017. The corporate alternative minimum tax (AMT) is repealed.
- 2. Pass-Thru Business Tax Rate** - The law creates a “business tax deduction” of 20% on “Qualified Business Income” for the owners of S corporations, partnerships and sole proprietorships. There are no further qualifications if the taxpayer’s income on their personal tax return does not exceed married filing joint \$315,000 or single \$157,500. If the taxpayer’s income exceeds these amounts, then this deduction is subject to the following additional limitations: (a) not available to **service business owners**, such as accountants and lawyers (**but not architects and engineers**), (b) other businesses are limited to 50% of your share of the W-2 wages of the business OR (c) **alternatively**, the limitation can be computed as 25% of your share of the W-2 wages paid by the business PLUS 2.5% of the original cost of property used in the production of income.
- 3. Expensing of Asset Acquisitions** – Instead of 50% bonus depreciation, taxpayers are able to fully and immediately expense 100% of the cost of qualified property (change in definition of “tangible personal property” including used property) acquired and placed in service **after September 27, 2017, and before Jan. 1, 2023.**
- 4. Code Sec. 179 Expensing** – Small business expensing of qualified property is increased to \$1 million (from the current \$500,000), and the phase-out amount is increased to \$2.5 million (from the current \$2 million), effective for tax years beginning after 2017 through tax years beginning before 2023. Both amounts will be indexed for inflation. The definition of section 179 property now includes tangible personal property to furnish lodging or in connection with furnishing lodging. This deduction now allows for “qualified real property” which include roofs, HVAC, fire protection and alarm systems and security systems acquired after the property was first placed into service.
- 5. Real Property** – The law maintains the current depreciation periods for both residential and non-residential real property (27.5 and 39 years respectively). It also eliminates the differences between qualified restaurant, qualified leasehold improvement, and qualified retail improvement properties. These costs should now be recovered over 15 years, but there was an error in drafting and they are currently deductible as 39-year property. Hopefully, Congress will fix this drafting error in technical corrections legislation.

6. **Meals & Entertainment** - The 50% limitation under current law now applies **not only to expenses for food or beverages and to qualifying business meals, but also to the expenses of the employer associated with providing food through an eating facility that meets the requirement for de minimis fringe**, with no deduction allowed for other entertainment expenses. Therefore, no deduction is allowed for entertainment, amusement or recreation activities, facilities, or membership dues relating to such activities or other social purposes. In addition, no deduction is allowed for transportation fringe benefits, benefits in the form of on-premises gyms and other athletic facilities, or for amenities provided to an employee that are primarily personal in nature and that involve property or services not directly related to the employer's trade or business.
7. **Net Operating Loss deduction limitation** – The law provides that taxpayers can only deduct a net operating loss (NOL) carryover or carryback to the extent of 80% of the taxpayer's taxable income (determined without regard to the NOL deduction) rather than the current 100% for small businesses. NOLs would have an indefinite carryforward period, but carrybacks would no longer be available for most businesses. Carryforwards for losses arising after 2018 would be increased by an interest factor.
8. **Qualified Production Activity Deduction** – The 9% deduction allowed for these activities are repealed for tax years beginning after 2018.
9. **Interest deduction limitations** – The law provides that every large business (with revenues in excess of \$25 million), regardless of its form, is subject to a disallowance of a deduction for net interest expense in excess of 30% of the business's adjusted taxable income. Disallowed interest deductions will be carried forward indefinitely and is applied at the taxpayer level. Not applicable to small businesses or businesses that utilize “floor plan” financing for qualifying inventory (vehicles, boats, farm machinery, etc. secured by such inventory). This also does not apply to real property trades.

This report only discusses the final proposals that we consider to be of general interest to business owners and is not a complete discussion of the law's contents. As with any changes in the tax laws, there are new planning opportunities to be considered. Please feel free to contact us with your specific questions.