

confidence
GAINED

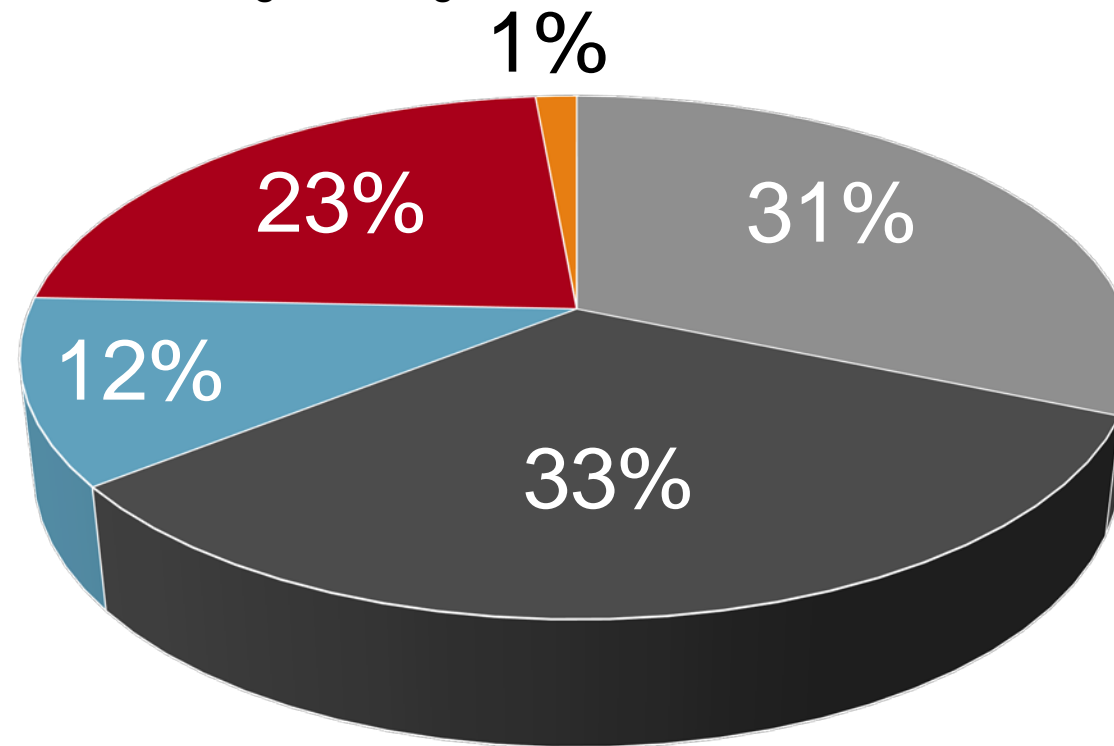


**GAINING MOMENTUM IN OUR
NEW TAX ENVIRONMENT:**
Moving Forward with Confidence

Sno L. Barry, CPA, MST
Cathy Jackson, CPA, MST



- Choice of entity after tax reform
- Depreciation and cost recovery
- Interest expense deduction
- Qualified business income deduction
- Repatriation of foreign earnings

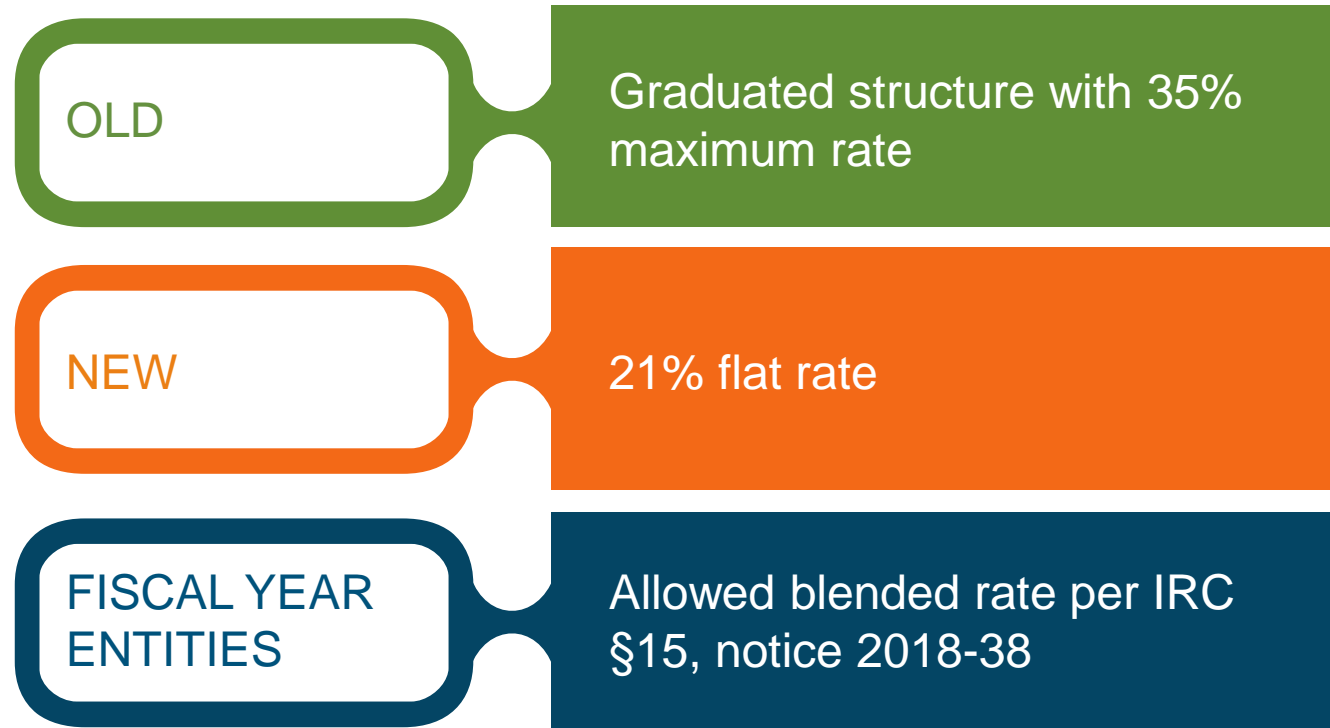


FEDERAL TAX REFORM

UNDERSTAND THE IMPACT OF TAX REFORM ON BUSINESSES

- 1** TAX RATE STRUCTURE FOR C-CORPORATIONS
- 2** TAX RATE STRUCTURE FOR PASS-THROUGH BUSINESSES
- 3** CHOICE OF ENTITY FOLLOWING REFORM
- 4** DEPRECIATION AND COST RECOVERY
- 5** INTEREST EXPENSE
- 6** OTHER BUSINESS DEDUCTIONS AND CREDITS

TAX RATE STRUCTURE FOR C-CORPORATIONS



ALTERNATIVE MINIMUM TAX FOR C-CORPORATIONS

OLD

20% on corporation's "alternative minimum taxable income" in excess of a \$40,000 exemption amount

NEW

AMT Repealed

ALSO: GENERAL BUSINESS CREDIT LIMITATIONS CONFORMED;
MINIMUM TAX CREDIT CARRYOVER REFUNDABLE

TAX RATE CHANGES FOR PASS-THROUGH ENTITIES

OLD & NEW

Income reported by owners or shareholders on individual tax returns at individual rates

NEW

20% Qualified Business Income (QBI) Deduction (*subject to limitations*)

2018

Rate	Single filers	Married filers filing joint
10%	\$0 - \$9,525	\$0 - \$19,050
12%	\$9,525 - \$38,700	\$19,050 - \$77,400
22%	\$38,700 - \$82,500	\$77,400 - \$165,000
24%	\$82,500 - \$157,500	\$165,000 - \$315,000
32%	\$157,500 - \$200,000	\$315,000 - \$400,000
35%	\$200,000 - \$500,000	\$400,000 - \$600,000
37%	Over \$500,000	Over \$600,000

2017

Rate	Single filers	Married filers filing joint
10%	\$0 - \$9,325	\$0 - \$18,650
15%	\$9,325 - \$37,950	\$18,650 - \$75,900
25%	\$37,950 - \$91,900	\$75,900 - \$153,100
28%	\$91,900 - \$191,650	\$153,100 - \$233,350
33%	\$191,650 - \$416,700	\$233,350 - \$416,700
35%	\$416,700 - \$418,400	\$416,700 - \$470,700
39.6%	Over \$418,400	Over \$470,700

QBI DEDUCTION

LESSER OF:

- A. Combined Qualified Business Income of taxpayer, or
- B. 20% of the excess of taxable income over sum of net capital gain

Combined Qualified Business Income

- 1. 20% of QBI, or
- 2. GREATER of:
 - a. 50% of allocable share of W-2 wages paid by entity, or
 - b. 25% of allocable share of W-2 wages, PLUS 2.5% of allocable share of unadjusted basis of the entity's assets

NOTE: W-2/ASSET LIMITATIONS IGNORED IF TAXABLE INCOME BEFORE QBI DEDUCTION < \$315,000 (MFJ) OR \$157,500 FOR ALL OTHER FILERS.

WHAT IS QBI?

Net amount of qualified income, gain, deductions and losses from a **Qualified Trade or Business**

NOTE: MUST BE EFFECTIVELY CONNECTED WITH U.S. TRADE OR BUSINESS

EXCLUDES:

1. Wages/guaranteed payments you earned from such entities
2. Certain investment income

TYPES OF ENTITIES THAT CAN HAVE QBI?

- S Corporations
- Partnerships (LLCs, LPs and General Partnerships)
- Sole Proprietorships- Schedule C
- Trusts and Estates
- Schedule E (maybe)

QUALIFIED TRADE OR BUSINESS

Every trade or business other than employee or specified service trade or business

QBI DEDUCTION

Specified service businesses prohibited

Brokerage
Services

Health

Actuarial Services

Consulting

“Any trade or business where the principal asset of such trade or business is the reputation or skill of 1 or more of its employees”

Law

Athletics

Accounting

Performing
Arts

Financial
Services

	NON-SERVICE INDUSTRY	SERVICE INDUSTRY
Taxable Income < \$315,000 MFJ, \$157,500 Single	20% Deduction	20% Deduction
Taxable Income > \$315,000 but less than \$415,000 (\$157,500 / \$207,500 Single)	Limitation Phased-In	Deduction Phase-Out
Taxable Income > \$415,000 MFJ, \$207,500 Single	W-2 / Property Limit Applies	0% Deduction



QBI DEDUCTION

A FEW MORE POINTS...

- Overall limitation: excess of taxable income over net capital gain income
- Doesn't increase an NOL

QBI DEDUCTION HAS LIMITATIONS

LESSER OF:

1. 20% of QBI, or
2. GREATER of:
 - a. 50% of allocable share of W-2 wages paid by entity, or
 - b. 25% of allocable share of W-2 wages, PLUS 2.5% of allocable share of unadjusted basis of the entity's assets

NOTE: W-2/ASSET LIMITATIONS IGNORED IF TAXABLE INCOME BEFORE QBI DEDUCTION < \$315,000 (MFJ) OR \$157,500 FOR ALL OTHER FILERS.

EXAMPLE 1

Taxpayer's Taxable Income (MFJ): \$250,000

QBI from Consulting: \$65,000

QBI Deduction is LESSOR of:

1. 20% of QBI $\$65,000 * 20\% = \$13,000$
2. 20% of taxable Income $\$250,000 * 20\% = \$50,000$

TAXABLE INCOME IS BELOW THE TAXABLE INCOME THRESHOLD

NO LIMITATIONS APPLY

EXAMPLE 2

Taxpayer's Taxable Income (MFJ):	\$450,000
QBI from Pass-through:	\$350,000
Allocable W-2 wages paid:	\$100,000
Unadjusted cost basis of Qualified Property:	\$600,000

Qualified Business Income Deduction is LESSOR of:

1. Lessor of:

20% of QBI

$$\$350,000 * 20\% = \$70,000$$

or

Greater of:

i. 50% of Wages

$$\$100,000 * 50\% = \$50,000$$

ii. 25% of Wages + 2.5% of Qualified Property

$$(\$100,000 * 25\%) + (\$600,000 * 2.5\%) = \$40,000$$

2. 20% of taxable income

$$\$450,000 * 20\% = \$90,000$$

TAXABLE INCOME IS ABOVE THE TAXABLE INCOME THRESHOLD

LIMITATIONS APPLY

EXAMPLE 3

Taxpayer's Taxable Income (MFJ):	\$370,000
QBI from Pass-through:	\$350,000
Allocable W-2 wages paid:	\$100,000
Unadjusted cost basis of Qualified Property:	\$ -0-

STEP 1: Computing as if TI < Threshold amount

Qualified Business Income Deduction is:

20% of QBI $\$350,000 * 20\% = \$70,000$

STEP 2: Computing as if TI > Threshold amount

Qualified Business Income Deduction is LESSOR of:

1. Lessor of:

a. 20% of QBI $\$350,000 * 20\% = \$70,000$

b. Greater of:

i. 50% of Wages $\$100,000 * 50\% = \$50,000$

ii. 25% of Wages + 2.5% of Qualified Property $(\$100,000 * 25\%) + (\$0 * 2.5\%) = \$25,000$

EXAMPLE 3

STEP 3: Computing “Excess Deduction” if no Limitation

	Step 1	\$70,000
Less:	Step 2	<u>(\$50,000)</u>
		<u>\$20,000</u>

STEP 4: Computing “Excess Taxable Income”

	Taxable Income	\$370,000
Less:	Taxable Income Threshold	<u>(\$315,000)</u>
		<u>\$55,000</u>

STEP 5: Computing “Phase-in %”

$$\begin{aligned} & \text{Excess Taxable Income} / \text{Total Phase-In Range} \times 100 \\ & = (\$55,000 / \$100,000) \times 100 \\ & = 55\% \end{aligned}$$

EXAMPLE 3

STEP 6: Computing "Final Deduction"

Deduction w/o limitation (Step 1)	\$70,000
Less: Excess Deduction (Step 3) x Phase-In %(Step 5)	
$\$20,000 \times 55\%$	<u>(\$11,000)</u>
	<u>\$59,000</u>

TAXABLE INCOME BETWEEN THE LOWER & UPPER TAXABLE INCOME THRESHOLD
PHASE-IN OF LIMITATION TO BE APPLIED



BUSINESS OWNERS

Choice of Entity Following Reform

PASS-THROUGH VS. C-CORP BEFORE TAX REFORM

C-CORP:

- Double taxation
- Top rate **50.47%**
 - 35% tax on earnings at business level
 - 23.8% tax on dividends at individual level
 - $(35\% + (65\% * 23.8\%)) =$
50.47%

PASS-THROUGH:

- Single level taxation
- Top individual rate **40.8%**
(includes impact of itemized deduction phase out for high earners)

10% TAX BENEFIT FOR PASS-THROUGH ENTITIES

PASS-THROUGH VS. C-CORP AFTER TAX REFORM

C-CORP:

- Double taxation
- Top rate **39.8%**
 - 21% tax on earnings at business level
 - 23.8% tax on dividends at individual level
 - $21\% * (79\% * 23.8\%) =$
39.8%

PASS-THROUGH:

- Single level taxation
- Top individual rate (new law) **37%**
- 20% QBI deduction
- $37\% * (\text{Less } 20\% \text{ deduction}) =$
29.6%

10% TAX BENEFIT FOR PASS-THROUGH ENTITIES

FACTORS TO CONSIDER

ELIGIBILITY FOR QBI DEDUCTION

- Nature of business
- Limitation on deduction

DISTRIBUTIONS VS. RETAINED EARNINGS

APPLICATION OF PAYROLL TAXES, SE TAXES, 3.8% MEDICARE SURTAX

STATE INCOME TAX DEDUCTION LIMITATION

BUSINESS INTEREST EXPENSE LIMITATION

DON'T FORGET TAX CONSEQUENCES OF CONVERSION...AND THE COST TO UNDO A CONVERSION



Depreciation and Cost Recovery

100% BONUS DEPRECIATION

- Assets placed in service after September 27, 2017
- Applies to new and USED property

Period	Applicable Percentage
9/27/2017 - 2022	100%
2023	80%
2024	60%
2025	40%
2026	20%
2027 - Forward	0%

SECTION 179

- Limitation increased to \$1 million max with \$2.5 million additions phase out
- Qualified Improvement Property qualifies for Section 179 (roofs, HVAC, security systems)

LUXURY AUTO DEPRECIATION

- Limits increased

LIKE-KIND EXCHANGES

- Limited to real property

QUALIFIED IMPROVEMENT PROPERTY

Any improvement to interior portion of a building that is nonresidential real property

Must be placed in service after the date the building was first placed in service

Currently 39 year recovery period *

Eligible for Section 179 but not bonus depreciation *

Excluding:

1. Enlargement
2. elevator/escalators
3. Internal structural framework



Interest Expense



BUSINESS INTEREST EXPENSE DISALLOWANCE IF:

- Interest expense $>$ 30% of business adjusted taxable income
- Adjusted taxable income is basically EBITDA
 - For 2018-2021 (adjustment for depreciation, amortization and depletion does not apply starting in 2022)
- Limitation does not apply to investment interest or floor plan interest

BUSINESS INTEREST EXPENSE DISALLOWANCE EXCEPTIONS:

- 3yr average gross receipts test < \$25 million
- Exception for certain trades or businesses:
 - An employee
 - Electing real property trade or business
 - Electing farming business
 - Regulated public utility
- Aggregation rules apply

BUSINESS INTEREST EXPENSE LIMITATION Section 163(j):

ELECTING REAL PROPERTY TRADE OR BUSINESS

Any real property development, redevelopment, construction, reconstruction, acquisition, conversion, rental, operation, management, leasing, or brokerage trade or business

ELECT OUT OF LIMITATION RULES

- Required to use ADS depreciation
- Not eligible for bonus depreciation
- Irrevocable election

ELECTING REAL PROPERTY TRADE OR BUSINESS

Asset Category	APPLYING INTEREST LIMITATION		ELECTING OUT OF INTEREST LIMITATION	
	Depreciable life (years)	Eligible for bonus?	Depreciable life (years)	Eligible for bonus?
Nonresidential real property	39	No	40	No
Residential rental property	27.5	No	30	No
Qualified improvement property – under tax reform	39	No	40	No
Qualified improvement property – if Congress passes a technical corrections bill	15	Yes	20	No
Most other tangible property	5 to 15	Yes	5 to 15	Yes



Other Business Deductions and Credits

- Net operating loss deductions
- Excess Business Losses
- Accounting Methods
- DPAD repealed
- Credit for employer-paid family medical leave
- Deduction for fringe benefit expenses limited
- Meals & Entertainment

BUSINESS MEALS & ENTERTAINMENT

	PRIOR LAW	NEW LAW 1/1/18
Client Entertainment	50% deductible	0% deductible
Client Meals	50% deductible	50% deductible
Employee Travel Meals	50% deductible	50% deductible
Meals for the Convenience of Employer	100% deductible if de minimis fringe benefit	50% deductible

QUESTIONS?



**SNO L. BARRY, CPA, MST
PRINCIPAL**
sbarry@berrydunn.com



**CATHY JACKSON, CPA, MST
MANAGER**
cjackson@berrydunn.com