Abbott, Stringham & Lynch

Tax Group

Understanding the New Tax Act

Presented by: Luis Ramirez, CPA
January 23, 2018

Abbott, Stringham & Lynch
CERTIFIED PUBLIC ACCOUNTANTS & BUSINESS ADVISORS

Upcoming Webinars
All at 12:00-1:00 PST

Thursday, January 25, 2018 - Tax Reform for Corporations and Businesses

Tuesday, January 30, 2018 - For Better or Worse? Individual Taxes Under the New Tax Reform Act

Thursday, February 1, 2018 - US Tax Reform: The Big Shake-up in International Tax Law

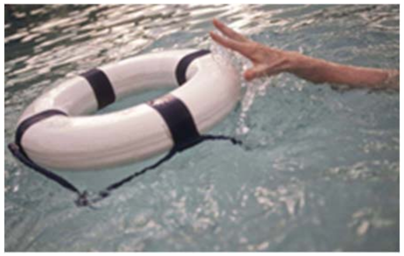
Tuesday, February 6, 2018 - Tax Reform and the Impact on Real Estate

Wednesday, February 7, 2018 - Tax Reform for Pass-Through Entities

Overview

- H.R. 1-- "An Act To Provide For Reconciliation Pursuant To Titles II and V Of The Concurrent Resolution On The Budget For Fiscal Year 2018"
- Political theme was tax decreases……. reality for some but not for all
- Wide ranging changes
- Largest change to tax system since 1986
- Projected to add $1.456 trillion to federal deficit 2018 to 2027
- Generally, effective January 1, 2018
  - Individual changes expire December 31, 2025
  - Business changes are permanent
- ACA penalty for no insurance eliminated after 2018 but net investment income tax still applicable
- California conformity ??
- More details in our webinar series

Individuals - Tax Savers



- Retain 7 tax brackets
  - 10%, 12%, 22%, 24%, 32%, 35%, and 37%
    - Imposes highest rate at $600,000 MFJ and $500,000 single and HOH
  - Widen brackets
- Increase standard deduction
  - Single $12,000
  - Joint $24,000
- Alternative Minimum Tax modified to impact fewer taxpayers
  - AMT triggers eliminated--exemptions, state/local tax, miscellaneous deductions, equity line interest

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Tax Reform Roadmap

Individual				
Topic	**Pre-Reform Law**	**2017 Reform Act**	**Act Sections**	**I.R.C. Sections**
Tax Rates	Individual Income Tax Rates For tax year 2017, there are seven regular individual income tax brackets of 10%, 15%, 25%, 28%, 33%, 35%, and 39.6%, and five categories of filing status. The income levels for each bracket threshold are indexed annually based on increases in the Consumer Price Index (CPI). Married Filing Jointly and Surviving Spouses: 10% (Taxable income not over \$18,650) 15% (Over \$18,650 but not over \$75,900) 25% (Over \$75,900 but not over \$153,100) 28% (Over \$153,100 but not over \$233,350) 33% (Over \$233,350 but not over \$416,700) 35% (Over \$416,700 but not over 470,700) 39.6% (over \$470,700) Married Filing Separately: 10% (Taxable income not over \$9,325) 15% (Over \$9,325 but not over \$37,950) 25% (Over \$37,950 but not over \$76,550) 28% (Over \$76,550 but not over \$116,675) 33% (Over \$116,675 but not over \$208,350) 35% (Over \$208,350 but not over \$235,350) 39.6% (over \$235,350) Head of Household: 10% (Taxable income not over \$13,350) 15% (Over \$13,350 but not over \$50,800) 25% (Over \$50,800 but not over \$131,200) 28% (Over \$131,200 but not over \$212,500) 33% (Over \$212,500 but not over \$416,700) 35% (Over \$416,700 but not over \$444,550) 39.6% (over \$444,550)	Individual Income Tax Rates The Act has seven tax brackets: 10%, 12%, 22%, 24%, 32%, 35%, and 37%. These brackets apply to tax years beginning after Dec. 31, 2017, and before Jan. 1, 2026 Married Filing Jointly and Surviving Spouses: 10% (Taxable income not over \$19,050) 12% (Over \$19,050 but not over \$77,400) 22% (Over \$77,400 but not over \$165,000) 24% (Over \$165,000 but not over \$315,000) 32% (Over \$315,000 but not over \$400,000) 35% (Over \$400,000 but not over 600,000) 37% (over \$600,000) Married Filing Separately: 10% (Taxable income not over \$9,525) 12% (Over \$9,525 but not over \$38,700) 22% (Over \$38,700 but not over \$82,500) 24% (Over \$82,500 but not over \$157,500) 32% (Over \$157,500 but not over \$200,000) 35% (Over \$200,000 but not over \$300,000) 37% (Over \$300,000) Head of Household: 10% (Taxable income not over \$13,600) 12% (Over \$13,600 but not over \$51,800) 22% (Over \$51,800 but not over \$82,500) 24% (Over \$82,500 but not over \$157,500) 32% (Over \$157,500 but not over \$200,000) 35% (Over \$200,000 but not over \$500,000) 37% (Over \$500,000)	§11001, §11002	§1, §15, §63(c)(2)(A)

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Tax Reform Roadmap-continued

Individual				
Topic	**Pre-Reform Law**	**2017 Reform Act**	**Act Sections**	**I.R.C. Sections**
Tax Rates (cont.)	Single Individuals: 10% (Taxable income not over $9,325) 15% (Over $9,325 but not over $37,950) 25% (Over $37,950 but not over $91,900) 28% (Over $91,900 but not over $191,650) 33% (Over $191,650 but not over $416,700) 35% (Over $416,700 but not over $418,400) 39.6% (Over $418,400) Capital Gains Tax Rates Short-term capital gains are taxed as ordinary income. For tax year 2017, taxpayers in the 10% and 15% tax brackets pay no tax on long-term gains on most assets; taxpayers in the 25%, 28%, 33%, or 35% income tax brackets face a 15% rate on long-term capital gains. For those in the top 39.6% bracket for ordinary income, the rate is 20%.	Single Individuals: 10% (Taxable income not over $9,525) 12% (Over $9,525 but not over $38,700) 22% (Over $38,700 but not over $82,500) 24% (Over $82,500 but not over $157,500) 32% (Over $157,500 but not over $200,000) 35% (Over $200,000 but not over $500,000) 37% (Over $500,000) The income threshold amounts for each rate bracket will be indexed for inflation using C-CPI-U in tax years beginning after Dec. 31, 2018. The requirement to index the amounts for inflation using the C-CPI-U would not expire. The bill would simplify the "kiddie tax". Capital Gains Tax Rates Under the Act, the breakpoints between the 0% and 15% rates and between the 15% and 20% rates are the same as the under present law. For tax years beginning in 2018, the rate thresholds are as follows: Married Filing Jointly (and Surviving Spouses): 15% Rate Threshold - $77,200 20% Rate Threshold - $479,000 Married Filing Separately: 15% Rate Threshold - $38,600 20% Rate Threshold - $239,500 Head of Household: 15% Rate Threshold - $51,700 20% Rate Threshold - $452,400 Other Individuals: 15% Rate Threshold - $38,600 20% Rate Threshold - $425,800		

Individuals - Tax Savers (continued)

- Election to defer income from stock based compensation
- Retains existing home sale gain exclusion rules
- 529 Education Saving Plans allow distributions of $10,000 annually for K-12 tuition
- Repeal phase out of itemized deductions

Individuals - Revenue Raisers

- Eliminate personal exemptions
- Reduce itemized deductions
  - State, local and sales tax limited to $10,000
  - Mortgage debt capped at $750,000 ($375K MFS); N/A to mortgages existing on or before December 15, 2017 - $1M threshold
  - No deduction for home equity loan interest
  - No miscellaneous itemized deductions
    - Investment advisor fees
    - Tax prep fees
    - Unreimbursed employee business expenses
    - Casualty losses (unless in disaster area)
  - Deductions retained for charitable contributions and medical expenses

Individuals - Revenue Raisers (continued)

- Eliminate deduction for moving expenses
- Post 2018 divorce alimony no longer deductible by payor or taxable income to recipient
- Eliminated IRA recharacterizations

Observations:

- Fewer taxpayers will claim itemized deductions
  - Higher standard deduction
  - Reductions in allowed itemized deductions
  - Loss of state and local tax deductions
- Lower tax rates and wider brackets
  - Higher taxable income due to reduced deductions
- Fewer taxpayers subject to AMT

Business Entities - Tax Savers

- C-Corp rate reduced to flat 21%
  - Rate increase if taxable income under $50K
  - Eliminates special tax rate for personal service corporations
- Repeal corporate Alternative Minimum Tax
- AMT credits refundable after 2017 through 2022
- More entities eligible to use cash method of accounting
- Increase Section 179 deduction limit to $1 million
- 100% bonus depreciation
  - Property acquired after Sept 27, 2017
  - New or used property

Business Entities - Revenue Raisers

- Beginning in 2022, R&D expenses to be capitalized and amortized over a 5 year period
- Repeal of domestic production activities deduction
- Like-kind exchanges limited to only real estate
- Repeal deductions for certain meals, entertainment expenses
- Limitation on deduction of interest expense
- Eliminate carry back of net operating losses
  - Carryforwards limited to 80% of taxable income
- No deduction for sexual harassment settlements subject to nondisclosure agreements

Observations:

- Evaluate:
  - Possible changes in tax reporting method
  - Review tax impact of reduced corporate rate vs pass-through rate – possible entity change
  - Expansion of bonus depreciation applies to real estate businesses; cost segregation and TPR more relevant

Pass-Through Entities - Tax Savers

- 20% deduction of qualified business income (QBI)
  - Limitations apply based on taxable income and type of trade or business
  - Applies to partnerships, LLC's, S-corporations or sole proprietorships
    - Service businesses limited
    - Increase in accuracy related penalties
- Repeal partnership technical termination upon ownership changes

Pass-Through Entities - Revenue Raisers

- Carried interest holding period increased to three years
- Loss limitation rules applicable to individuals - $500K limitation

Observations:

- Evaluate impact of 20% deduction for QBI vis-à-vis loss of state tax deduction
- Planning opportunities for 20% QBI deduction
- Evaluate $500K limitation from all pass-through entities

International - Tax Savers

- 100% dividend received deduction for foreign source portion of dividends received from CFC's and 10% owned foreign corporations
  - No FTC or deduction is allowed for taxes paid or accrued
- Deduction for foreign derived intangible income (FDII)
  - Allows a 37.5% deduction for foreign source income
- $FDII =$

$$Deemed\ intangible\ income\ x\ \frac{foreign\ derived\ deduction\ eligible\ income}{total\ deduction\ eligible\ income}$$

International - Revenue Raisers

- Repatriation tax on deferred income
  - US shareholder of foreign corporation must include in income post 1986 earnings and profits beginning in 2017
    - Tax can be paid over 8 years with proper election
    - Tax on E&P at 15% for cash equivalents – all others 8%
- Global intangible low – taxed income (GLTI)
  - Foreign income that is taxed at 13.125% or less
    - New AMT?

Observations:

- Assess post 1986 E&P for foreign owned corporations
- Evaluate foreign effective tax rate for low taxed income for GLTI purposes
- Evaluate sources of foreign derived income where FDII deduction is available

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Estate, gift and generation skipping tax provisions

- Applicable exclusion doubled to $11.2M per person – up from $5.1M
- Re-evaluate existing estate plan