Abbott, Stringham & Lynch

Tax Group

Tax Reform for Corporations and Businesses

Presented by:

Rob Trammell, CPA and
Luis Ramirez, CPA

January 25, 2018

Abbott, Stringham & Lynch

CERTIFIED PUBLIC ACCOUNTANTS & BUSINESS ADVISORS

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

Tuesday, January 30, 2018 - For Better or Worse? Individual, Estate, and Trust 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

Agenda

- New Corporate Tax Rate and Impact on Flow-Through Entities
- The Loosening of Cash Basis Reporting for Tax Purposes and What That Means
- New Rules for Expensing Capital Equipment
- Other Items – time allowing

New Corporate Tax Rate and Impact on Flow-Through Entities

Old Rule:

- 15% for \$0 - \$50,000 of taxable income,
  25% for \$50,001 - \$75,000 of taxable income,
  34% for \$75,001 - \$10,000,000 of taxable income,
  35% for excess of \$10,000,000 of taxable income.

New Rule:

- A flat 21% effective for tax years beginning after 12/31/17.
- Fiscal year taxpayer.
- Personal service corporations - 21%

New Corporate Tax Rate and Impact on Flow-Through Entities (continued)

- Should you consider converting S corporation to C Corporation?
- The biggest reason to set up S corporation is to avoid double taxation.
- Will it still be a tax saving choice?
- General discussion regarding pass-through deduction.

New Corporate Tax Rate and Impact on Flow-Through Entities (continued)

Tax under the new rule (highest tax bracket used for illustration):

- C Corporation: Federal 21% + CA 8.84% = 27.98% (after state tax benefit)
- Pass-through entity: Federal 37% + CA 12.3% = 41.90% (after pass-through deduction)
- Tax savings on converting to C Corporation: 41.90% - 27.98% = 13.92%
- Is this the end of the discussion?

New Corporate Tax Rate and Impact on Flow-Through Entities (continued)

- C Corporations still have double taxation. Need to consider tax upon dividends, sale, etc.
- Section 199A deduction is complicated and you may not qualify. (More detail on this topic will be presented in an upcoming webinar.)
- Consult us for exact application of this as your facts and circumstances will dictate entity choice.

The Loosening of Cash Basis Reporting for Tax Purposes and What That Means

New qualification for cash method of accounting:

- Average gross receipts less than $25 million regardless of entity structure or industry compared to $5 million requirement previously.
- Repeals the requirement that corporations and partnerships with corporate partners satisfy the average annual gross receipts requirement for all prior years.
- More small to mid-sized corporations will be eligible to use cash basis accounting for tax reporting purposes.

The Loosening of Cash Basis Reporting for Tax Purposes and What That Means (continued)

- Taxpayers who meet the $25 million requirement will be excluded from the uniform capitalization rules of Section 263A.

- Taxpayers who meet the $25 million requirement will be exempt from the requirement to account for inventories. (Treat either as materials or supplies.)

- Application of the above provisions is considered a change in method of accounting under Section 481.

The Loosening of Cash Basis Reporting for Tax Purposes and What That Means (continued)

- Taxpayers who meet the $25 million requirement will be exempt from using the percentage-of-completion accounting method for long-term contacts. (Completed-contract method instead)

- Application of the above provision is NOT a change in method of accounting under Section 481.

- Effective for contracts entered into after 12/31/17, in taxable years ending after such date.

New Rules for Expensing Capital Equipment

- Bonus Depreciation:
- Current law – for 2017 could deduct 50% of cost of qualified new property. For 2018 would have been able to deduct 40% of cost of qualified new property.
- New law – 100% expensing for qualified property placed in service on and after 9/27/2017 before 1/1/2023
- The expensing percentage will drop 20% every year starting 1/1/2023 with complete phase-out after 1/1/2027.

New Rules for Expensing Capital Equipment (continued)

- Qualified property:
  - Tangible property with a recovery period of 20 years or less and certain computer software.
  - Used property also qualifies, however, property used in a real estate trade or business is excluded.
- Option to elect out of bonus depreciation.

New Rules for Expensing Capital Equipment (continued)

- Increases the deduction amount under §179 to $1 million.
- Increases the phase-out threshold to $2.5 million.
- The Act also expands the definition of qualified real property to include all qualified improvement property and certain improvements made to nonresidential real property.

Other Items

- Full repeal of corporate AMT.

- Modification of the net operating loss deduction – old law – 2 year carryback and 20 year carryforward. New law - no more carryback, carryforward indefinite, utilized loss limited to 80% of taxable income….be careful! (only applies to NOL’s generated after 12/31/2017).

- Interesting….under current law we can deduct expenses that are ordinary and necessary with certain exceptions. The new law disallows any deduction for a settlement, payout and attorney fees related to sexual harassment if subject to a nondisclosure agreement.

Other Items (continued)

- Limitation on business interest expense deduction to 30% of business adjusted taxable income. Taxpayers whose average annual gross receipts for the 3 prior taxable years are less than $25 million are exempt.
- Repeal of domestic production activities deduction (DPAD).
- Treatment of self-created property: no more capital gain treatment.
- Research and experimental expenditures: Capitalize and amortize R&D expense over 5 years. Fifteen years for activities outside of United States starting for years beginning after 12/31/2021.

Tax Reform for Corporations and Businesses

- Questions?