

HOW IS TAX REFORM AFFECTING YOUR PRACTICE

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Tax Reform

- **Public Law 115-97**
- **December 22, 2017**
 - Many provisions expire after 2025 (w/o further legislation)



Individuals –Tax Rate Reduction (generally)

2017 Brackets - MFJ		2018 Brackets- MFJ	
▪ 10%	\$0-18,650	10%	\$0-\$19,050
▪ 15%	\$18,651-\$75,900	12%	\$19,051-\$77,400
▪ 25%	\$75,901-\$153,100	22%	\$77,401-\$165,000
▪ 28%	\$153,101-\$233,350	24%	\$165,001-\$315,000
▪ 33%	\$233,351-\$416,700	32%	\$315,001-\$400,000
▪ 35%	\$416,701-\$470,700	35%	\$400,001-\$600,000
▪ 39.6%	\$470,701 and up	37%	\$600,001 and up



Tax Law Changes - Individuals

■ Standard Deduction

■ Old Law

- \$6,500 (Individual filer)
- \$9,550 (Head of Household)
- \$13,000 (Married filing Jointly)

■ New Law

- \$12,000 (individual filer)
- \$18,000 (Head of Household)
- \$24,000 (Married filing Jointly)



Tax Law Changes - Individuals

■ Personal Exemption

- Old Law - \$4,050 for yourself, spouse and each dependent.
- New law - **\$0**



Tax Law Changes - Individuals

■ Child Tax Credit

- Increased from \$1,000 per qualifying child under the age of 17 to \$2,000 per qualifying child under age 17.
- Credit begins to phase out at modified AGI of \$400,000 for MFJ and \$200,000 for all others.
 - **Under the old law the phase out began at \$110,000 (MFJ) and \$75,000 (all others).**
- Maximum portion refundable is increased from \$1,000 to \$1,400.



Tax Law Changes - Individuals

■ Mortgage Interest

- Old Law – up to \$1,000,000 + \$100,000 home equity loans
- New Law – *New* mortgages are capped at \$750,000. If loan was closed upon before December 15, 2017 the limit will still be \$1 million.
 - **Home Equity interest deduction was suspended for tax years 2018-2025.**



Tax Law Changes - Individuals

- **State and Local Tax Deductions**
 - Old Law – Deduct on Schedule A payments of state and local income taxes, sales tax, and property taxes paid in the year;
 - New Law – same taxes apply, but everything collectively is capped at \$10,000



Tax Law Changes - Individuals

■ Charitable Deductions

- Old Law – limited charitable deductions to 50% of Adjusted Gross Income (AGI);
- New Law – charitable contributions are limited to 60% of AGI



Tax Law Changes - Individuals

- **Miscellaneous Itemized Deductions (Schedule A)**
- **Old Law – Deduction available for expense totaling more than 2% of your AGI (including unreimbursed employee expenses, home office expenses, tax preparation expense, investment fees, safe deposit box fees).**
- **New Law – deductions are suspended (2018-2025).**



Tax Law Changes - Individuals

■ Pease Limitation

- Overall deductions from Schedule A under old law were limited by 3% for certain upper income taxpayers.
- New law suspends this limitation for tax years 2018-2025.



Tax Law Changes - Individuals

■ Above the Line Deductions

- Old Law – Student Loan Interest, Moving Expenses, Alimony, teacher supplies expenses were all deductible (not an itemized deduction)
- New Law – Student loan interest and teacher supply expense are retained, but Moving expense deduction is repealed (except for military personnel). Alimony is repealed beginning in 2019 for divorces finalized after December 31, 2018 (or modified after same date).



Tax Law Changes - Individuals

■ More on Moving Expenses

- Under old law companies could have provided moving expense reimbursements on a tax free basis to employees (within the constraints of the law).
- Under the new law these payments will generally be taxable.



Tax Law Changes - Individuals

■ 529 Plans

- Old Law – Distributions from plans could be used for costs associated with college – tuition, room and board, fees, books, supplies and equipment, and be free from federal tax (including the earnings).
- New Law – expands the permitted use to public, private, and religious - elementary and secondary schools as well as colleges.



Tax Law Changes - Individuals

■ Estate and Trust Tax Rates

■ Bracket:

<u>Taxable Income</u>	<u>Tax Due is:</u>
○ \$0-2,550	10% of Taxable Income
○ \$2,551-\$9,150	\$255 + 24% of amount over \$2,550
○ \$9,151-\$12,500	\$1,839 + 35% of amount over \$9,150
○ \$12,501 +	\$3,012 + 37% of amount over \$12,500



Tax Law Changes - Individuals

- **Federal Estate Tax Exemption Amount**

- For 2018 - \$11,180,000 (will increase w/ inflation) per person

- **Gift Tax Exemption Amount**

- For 2018 this amount is \$15,000 (gift tax free – per person, per year).



Tax Law Changes - Individuals

■ Individual Alternative Minimum Tax

- This was retained under the new law, but the exemption amount was increased to \$109,400 (MFJ) from 84,500 (2017).
- Many taxpayers will not pay AMT for 2018 because there were many nondeductible items for AMT purposes that were simply disallowed under the new law.



Tax Law Changes - Businesses

- **Old Law (Pre 2018)**

- C Corporations paid tax at graduated rates. As income rose – so did tax rate.

<i>Income</i>	<i>Rate</i>
▪ 0-\$50K	15%
▪ 50-75K	25%
▪ \$75-10M	34%

- **New Law – all income is taxed at 21%**
- **This change is “permanent” – no sunset in the law.**
- **Rates on Personal Service Corporations is eliminated.**



TAX LAW CHANGES – BUSINESSES

C - CORPORATION

- **"Double Taxation"**

- Dividends from a C Corporation are also taxed to the shareholders, thereby creating 2 levels of Tax.
- Amount of Tax (and rate) will depend upon individual level of shareholder income. (2018 *illustrated below*).

Tax Rate - Dividends	Single	Married-Jtly	Head of Household	Estate/Trust
0%	Up to \$38,599	Up to \$77,199	Up to \$51,699	\$2,599
15%	\$38,600 to \$425,799	\$77,200 to \$478,999	\$51,700 to \$452,399	\$2,600-\$12,699
20%	\$425,800 and up	\$479,000 and up	\$452,400 and up	\$12,700 and up

TAX LAW CHANGES – BUSINESS C CORPORATION VS. PASSTHROUGH

	C Corporation	Pass-through
▪ Income	\$100	\$100
▪ <u>Entity Fed Tax</u>	<u>\$21</u>	<u>\$0</u>
▪ Dividend	\$79	NA
▪ <u>Shareholder Tax</u>	<u>\$15.8</u>	<u>\$37</u>
▪ Net to shareholder	\$63.20	\$63

Tax Law Changes - Businesses

- **New Section 199A added to provide some benefit to owners of pass through entities (S corporations, sole proprietorships and tax partnerships) since businesses organized as C corporations were benefiting with the lower 21% flat tax rate.**
- **Very complicated in its application.**
- **Good from 2018 until tax year 2025; sunset thereafter.**
- **If taxpayer qualifies it could provide a deduction equal to up to 20% of pass-through income.**
- **Income earned as an employees is not eligible. Likewise Guaranteed Payments are not eligible.**
- **Trusts and estates are eligible.**
- **The deduction is not an above the line deduction but does reduce taxable income (but not AGI)**



Tax Law Changes - Businesses

- **If Taxpayer is eligible for the pass through deduction, effective tax rate from pass through income drops significantly:**

- Highest Individual rate 37%
- 20% Pass Through Deduction (7.4%) (20% of 37%)
- Effective Tax Rate **29.6%**



Tax Law Changes - Businesses

- **Eligibility for Deduction – complex for higher income earners.**
 - Over \$315,000 (joint filers); \$157,500 other filers.
 - Below these amounts – no great scrutiny.



Tax Law Changes - Businesses

- **Pass Through Deduction**
- **Limitations**
 - Is it a Specified Service Trade or Business
 - Greater of 50% of W-2 Wages or
 - Sum of 25% of W-2 Wages + 2.5% of Unadjusted Basis immediately after acquisition (UBIA) of all qualified property (generally tangible personal property).



Tax Law Changes - Businesses

- **1031 Exchanges (like-kind exchanges)**
- **Old Law – Real and tangible/intangible property were eligible for the deferral of taxation of gain from sale/exchange of property.**
- **New Law – Only eligible for real property sale/exchanges.**



Tax Law Changes - Businesses

- **Depreciation/Expenses**
- **Old Law – Under Section 179 up to \$500,000 was available to expense per year for property placed in service; Phase out at \$2,000,000.**
- **New Law - \$1,000,000 limit. Increased phase out at \$2.5 million.**
 - Section 179 was expanded to also include additional property (qualified improvement property), roofs, alarm/security systems.



Tax Law Changes - Businesses

- **Temporary 100 percent Expensing (bonus depreciation)**
- **Old law – 50%/40%**
- **New law – 100% for qualified property acquired and placed in service after September 27, 2017 and before January 1, 2023.**
 - Now ‘used’ property also qualifies, with certain exceptions.
 - Certain type of property are not eligible for bonus depreciation – property primarily used in electrical energy, water sewer disposal services, etc.



Tax Law Changes - Businesses

- **Cash Basis of Accounting**

- New law expands those businesses that are eligible for cash basis reporting to businesses with average annual gross receipts of less than \$25 million in prior 3 years.



Tax Law Changes - Businesses

■ Sale of Self Created Property

- Gains from certain sales of self-created property (patents, inventions, designs) will not be treated as capital gains.

■ Sexual Harrassment Settlement Payments

- If payments after 12-22-2017 are conditioned upon non-disclosure agreement – deductions are not permitted.



Tax Law Changes - Businesses

■ Interest Deduction Limitation

- 30% of “Adjusted” Taxable Income
 - **Before 2021**
 - **After 12/31/2021 (Tax Year 2022 +)**
- Any Interest not deductible can be carried forward indefinitely.
 - **Exemptions from the limitation**
 - \$25 million in gross receipts
 - Regulated utilities



Tax Law Changes - Businesses

- **Corporate AMT is repealed beginning in 2018**
- **For 2018, 2019 and 2020 to the extent AMT credit carryover exceed regular tax liability, generally 50% of the excess AMT credit carryover will be refundable;**
- **In 2021 any remaining AMT credit carryover will be refundable.**



Tax Law Changes - Businesses

■ Net Operating Loss Deductions

- “Old” Rule – 2 years to carry back; 20 year carry forward. Still in place for NOLs arising from tax years ending before 1/1/2018.
- New Rule – NOLs arising in tax years after 12/31/2017 may not be carried back; indefinite carryforward.
 - **80% limitation rule – NOLs arising after 12/31/2017 are limited to 80% of taxable income. (No limitation on NOLs arising under Old Rule.**



Tax Law Changes - Businesses

- **Profits Interest / Carried Interest Rules**
 - Section 1061
 - **3 year holding period for long term capital gain treatment**
 - **Applicable partnership interest.**
 - **Applicable trade or business**



Tax Law Changes – Individuals/Business

- **New Loss Limitation Rule (Active Losses)**
 - Excess Business Losses are limited (disallowed);
 - Excess of business deductions over business income plus a threshold amount of \$250,000 or \$500,000 for MFJ filers.
 - \$500,000 limit is indexed for inflation.
 - Non-deductible losses are carried-forward as part of NOL of taxpayer.
 - Applies after passive loss rules are applied.



THANK YOU

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