Navigating Tax Reform for Private Sector Businesses

Leslie Boyd, Principal

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WEALTH ADVISORY | OUTSOURCING | AUDIT, TAX, AND CONSULTING

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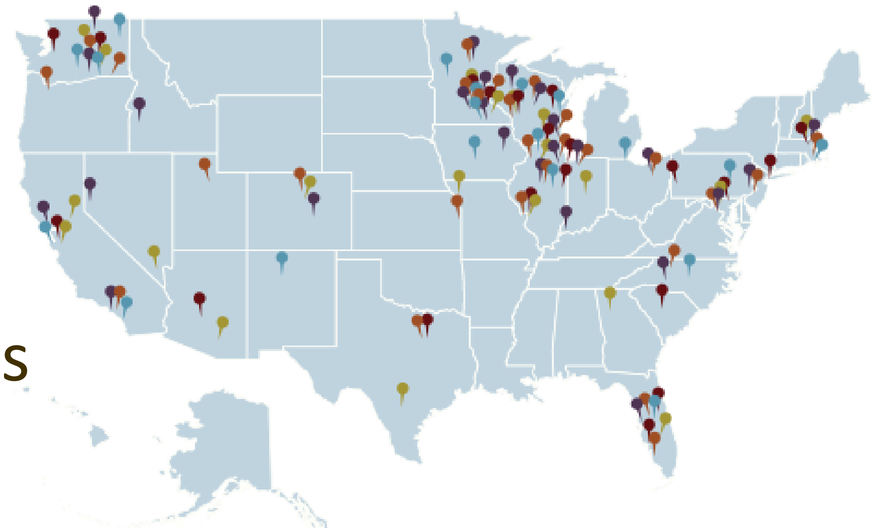

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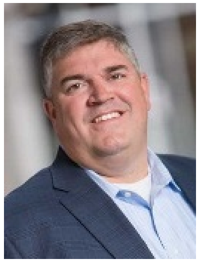
Speaker Introductions

Leslie Boyd, Principal

Leslie has more than ten years of experience in public accounting and has prepared and reviewed complex federal and state tax returns for C corporations, S corporations, partnerships, and individuals. Leslie is the Indianapolis Federal Tax Solutions Leader which includes managing Research and Development studies as well as other consulting projects. She works with clients across a wide spectrum from small manufacturers to large public companies.



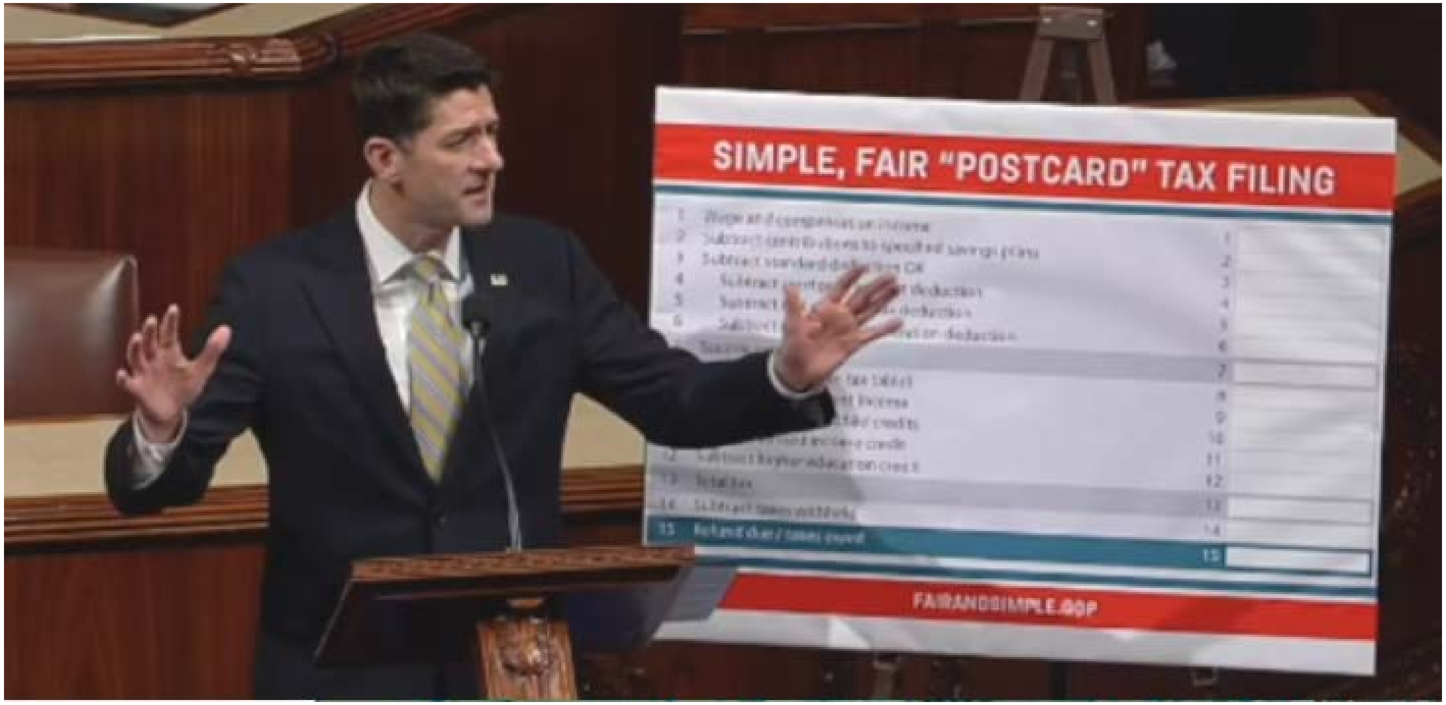
Kevin Cox, Managing Principal of Tax

Kevin is a principal at CLA and brings more than 20 years of experience in the accounting field. He dedicates a majority of his time providing unique tax strategies and tax savings opportunities customized to the needs of each client. Kevin's diverse background includes being the regional tax principal-in-charge of the CLA Western region for the past four years as well as on the tax executive team as the managing principal of industries for one of the largest accounting firms in the United States.

Learning Objectives

- At the end of this session, you will be able to:
  - Identify key points related to the new tax plan
  - Understand how tax reform impacts you and your business
  - Develop planning strategies relevant to your business and personal tax situation

Key takeaway: Today we are presenting tax reform at a very high level. You may have specific questions about how it affects you and your business. Feel free to submit your questions during the webinar or in the post-event evaluation.



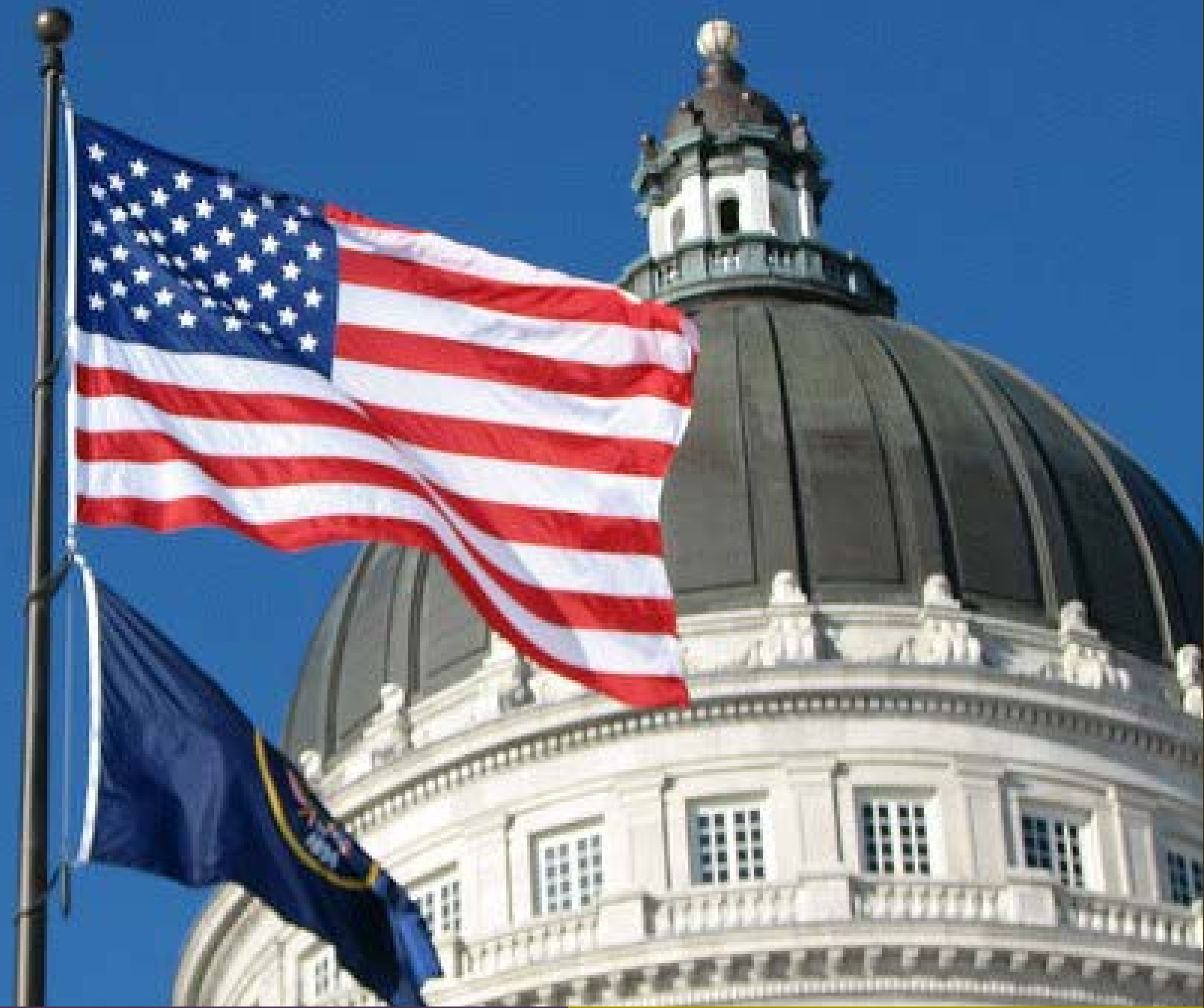
How hard can it be?

H.R.1 – Tax Cuts and Jobs Act (TCJA)

- **H.R.1 Official Title:** "An Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018."
- **December 22, 2017:** Signed into law by President Trump (Public Law No. 115-97)

Tax Cuts and Jobs Act (TCJA)

Key Aspect Comparison:
Tax Rates



Individual Tax Rates

2017 Individual Tax Rates (Pre-TCJA)

Tax Bracket	Single	MFJ	H of H
10%	9,325	18,650	13,350
15%	37,950	75,900	50,800
25%	91,900	153,100	131,200
28%	191,650	233,350	212,500
33%	416,700	416,700	416,700
35%	418,400	470,700	444,550
39.6%		**EXCESS**	

2018 – 2025* Individual Tax Rates (Under TCJA)

Tax Bracket	Single	MFJ	H of H
10%	9,325	19,050	13,600
12%	38,700	77,400	51,800
22%	82,500	165,000	82,500
24%	157,500	315,000	157,500
32%	200,000	400,000	200,000
35%	500,000	600,000	500,000
37%		**EXCESS**	

* Barring further legislation, the TCJA individual rate changes will expire (sunset) after 2025.

Corporate Tax Rates

2017 Corporate Tax Rates (Graduated)	
Tax Bracket	**Taxable Income**
15%	50,000
25%	75,000
34%	100,000
39%	335,000
34%	10,000,000
35%	15,000000
38%	18,333,333
35%	**EXCESS**
Corporate AMT Tax Rate = 20%	

Corporate Tax Rate Under TCJA:

- **Flat 21% Rate, effective for tax years beginning after December 31, 2017***
- **20% Corporate AMT Repealed** *(Prior AMT Credits refundable up to 50% of excess AMT credits > regular tax liability for 2018 – 2020; Remaining AMT credit refunded in 2021.)*

*Blended tax rate for corporations with fiscal years beginning before 12/31/2017.

Capital Gains Tax Rates

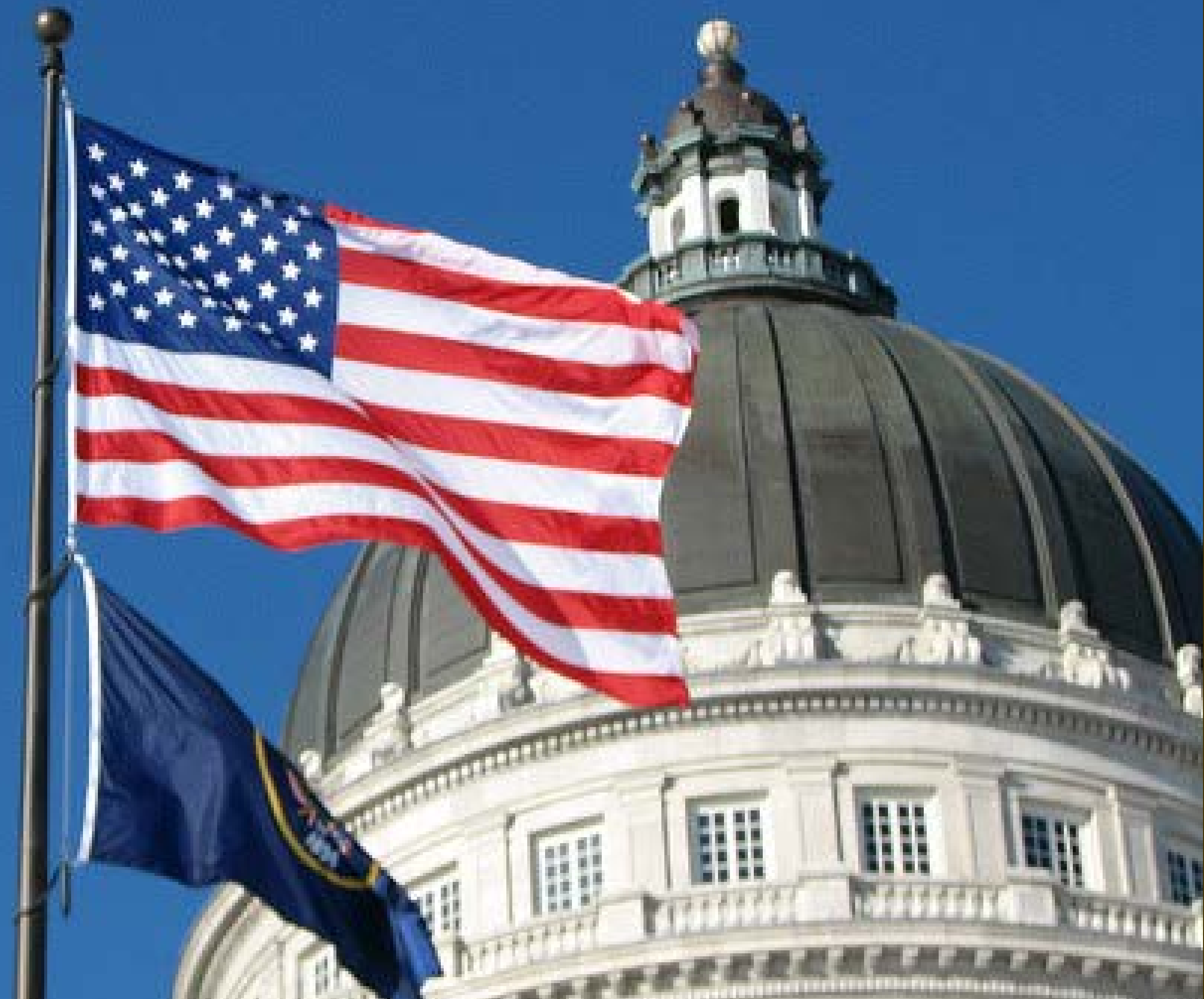
2017 Capital Gains Tax Rates (Pre-TCJA)				
Tax Bracket	**Single**	**MFJ**	**H of H**	**Estates & Trusts**
0%	37,950	75,900	50,800	2,550
15%	418,400	470,700	444,550	12,500
20%	**EXCESS**			

2018 – 2025* Capital Gains Tax Rates (Under TCJA)				
Tax Bracket	**Single**	**MFJ**	**H of H**	**Estates & Trusts**
0%	38,600	77,200	51,700	2,600
15%	425,800	479,000	452,400	12,700
20%	**EXCESS**			

- **TCJA generally retains prior law tax rates and breakpoints on capital gains and qualified dividends.**
  - *Breakpoints at which the 15% and 20% tax rates begin to apply are indexed for inflation for tax years after December 31, 2017.*
- **Ordinary income fills lower brackets first, then capital gains.**
  - *Deductions offset ordinary income.*

Tax Cuts and Jobs Act (TCJA)

Key Aspect Comparison: ***Individual Provisions***



Individual Tax Deductions

Tax Bracket	Pre-TCJA	Under TCJA
Standard Deduction	Single: 6,350 MFJ: 12,700 HoH: 9,350	Single: 12,000 MFJ: 24,000 HoH: 18,000
Personal Exemption	$4,050 per Individual **Subject to AGI Phase-out*	*Repealed*
Mortgage Interest	Debt Limit: $1.1M 2nd Home Allowed: Yes Home Equity Interest Allowed: Yes	Debt Limit: $750,000 2nd Home Allowed: Yes Home Equity Interest Allowed: No
Taxes	<u>Itemized Deduction Allowed for:</u> • Real Estate Tax (U.S. Property Only) • Personal Property Tax • State/Local Income Tax (or sales tax) **Subject to AGI Phase-out*	Itemized Deduction **Limited to $10,000** for the *Aggregate* of State & Local Property and Income Taxes
Charitable Deductions	Limited to 50% AGI	Limited to 60% AGI **80% Deduction for Athletic Tickets Repealed*
Miscellaneous Deductions	Itemized Deduction Subject to 2% AGI Floor (includes employee business expense, investment expenses, tax prep fees, professional dues, etc.)	*Repealed*
Medical Expenses	Subject to 10% AGI Floor	Subject to 7.5% AGI Floor **Retroactive to 2017*
AGI Phase-out	Phase-out begins at $313,800 (MFJ)	*Repealed*

Other Individual Provisions

- Child Tax Credit Increased from $1,000 to $2,000
- American Opportunity Tax Credit Retained
- Alimony Changes:
  - No longer deductible by payor
  - No longer included in income by payee
  - Applies to divorce/separation agreements executed after 12/31/2018
- Exclusion for Moving Expense Reimbursements Suspended Until 2026
  - Does not apply to members of the Armed Forces on active duty who moved pursuant to military order
  - *Moving Expense Deduction – Suspended Until 2026*
- Individual Mandate Under ACA Repealed
- Individual AMT Retained – Exemptions Increased

Individual Qualified Business Income (QBI) Deduction

- Under pre-TCJA, no special deduction for QBI
- Deduction available for noncorporate taxpayers
  - o *Also referred to as the "pass-through deduction"*
- Not a deduction to arrive at AGI
  - o *Does not reduce AGI for purposes of AGI thresholds*
- Intended to reduce the tax rate on QBI to a rate closer to the corporate tax rate
- 20% accuracy penalty applies when understatement exceeds 5%
  - – Normally applies to understatement > 10%
- *Sunsets for tax years beginning after 12/31/2025*

Individual Qualified Business Income (QBI) Deduction

- Deduction = 20% Non-Wage Business Income
    - Sole Proprietorships (reported on Schedule C)
    - Pass-through entities subject to tax at the individual owner level (from Schedule K-1)
    - *Wages paid by S corporation and guaranteed payments paid by partnership not included*

Individual Qualified Business Income (QBI) Deduction

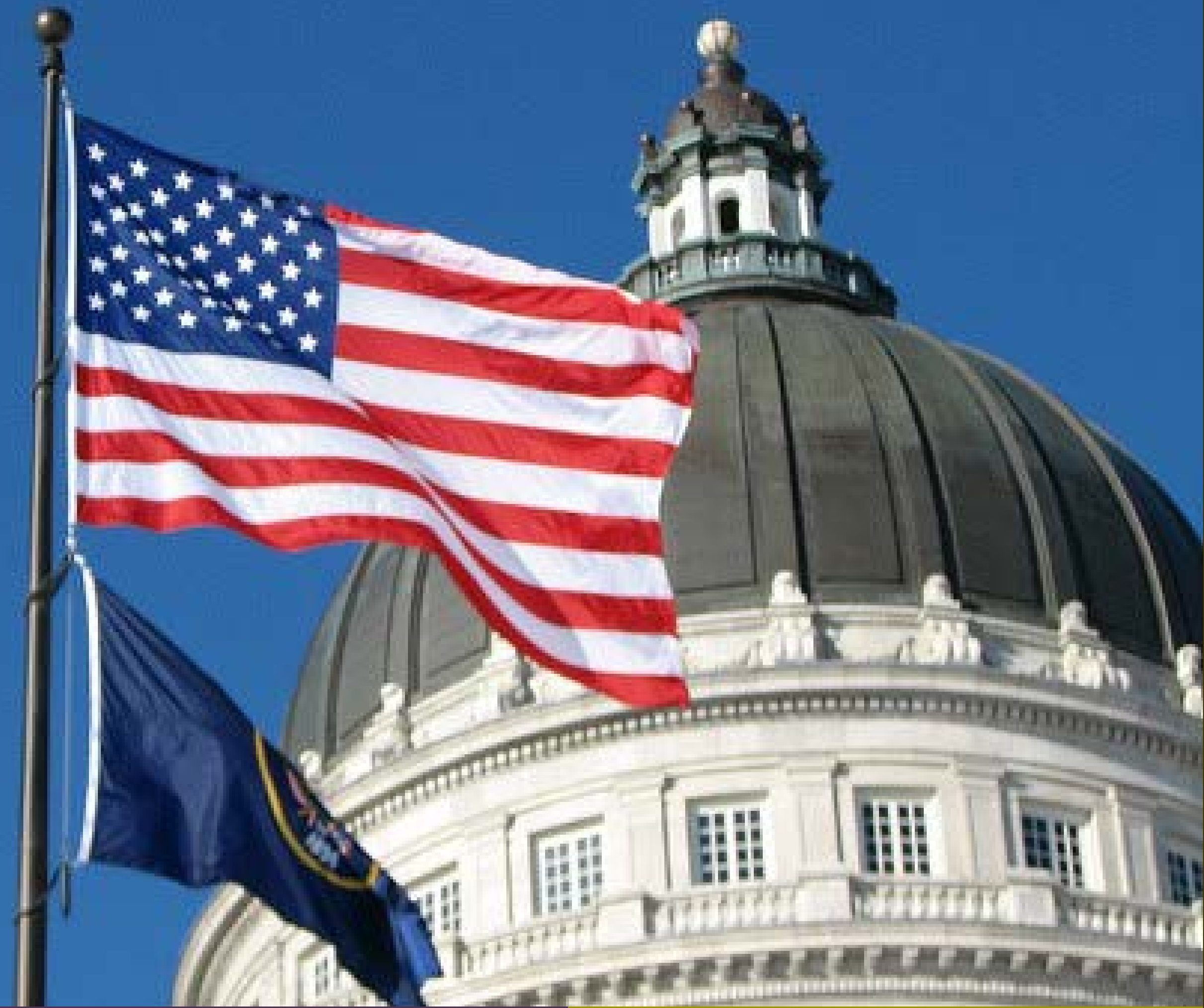
- **Limited to greater of:**
  - 50% of the taxpayer's share of allocable wages from pass-through entities
  - Sum of 25% allocable wages +2.5% unadjusted basis of qualified property
- **Qualified Property Defined:**
  - Depreciable tangible property held by and available for use at the close of the tax year
  - Included in computation if held at least 10 years or until expiration of recovery period, whichever is longer

Individual Qualified Business Income (QBI) Deduction

- Lower Income and Wage Limitation
  - Wage and investment limitation does not apply for taxpayers below taxable income threshold amounts
    - <$315,000 MFJ/$157,500 Single
    - Phase in 20% limit over next $100,000 MFJ/$50,000 Single
- Deduction Allowed Against AMTI
- Not Available for Purposes of Self-Employment Tax
- Deduction Allowed to Non-Itemizers

Tax Cuts and Jobs Act (TCJA)

Key Aspect Comparison: *Business Provisions*



Bonus Depreciation

- Pre-TCJA: 50% Bonus Depreciation On New Property Placed in Service During 2017
  - Scheduled to phase down to 40% in 2018, 30% in 2019, and zero thereafter
- Under TCJA: 100% Bonus Depreciation
  - Applied retroactively and effective for property acquired and placed in service after September 27, 2017
  - Phase down beginning in 2023 (fully phased out after 2026)
  - Eligibility expanded to used property

Section 179 Expensing

- **Pre-TCJA: Section 179 Expensing Limited to $510,000 (for tax years beginning in 2017)**
  - Asset addition phase-out limit for 2017 begins at $2,030,000
  - HVAC units only available for Section 179 if treated as "personal property"
- **Under TCJA: Section 179 Expensing Limit Increased to $1M**
  - Phase-out threshold increased to $2.5M
  - Eligibility expanded to include roofs, HVAC and fire alarm/security systems.
  - Effective for tax years beginning after 12/31/2017

Disallowed Business Interest Expense

- **Pre-TCJA:** Business interest generally allowed as a deduction
- **Under TCJA:** Interest expense limited to interest income + 30% of remaining adjusted taxable income
  - Remaining business adjusted taxable income
    - Determined w/o interest income, NOL, 199A, depreciation, amortization, depletion
    - Determined at tax filer level (1065, 1120-S, 1120)
  - Excess carried forward indefinitely
  - ***Businesses with <$25M average annual gross receipts exempt***

Section 199: Domestic Production Activities Deduction

- **Pre-TCJA:** Section 199 allows a deduction of 9% of the taxpayer's qualified production activities income for the tax year

- **Under TCJA:** *Repealed*
  - Effective for taxable years beginning after 12/31/2017

Meals and Entertainment

- **Entertainment Expense: Non-Deductible!**
  - o Transportation passes and parking fringes disallowed
  - o Social, athletic and sporting clubs treated as entertainment
- **Employer-provided eating facility limited to 50%**
  - o *Pre-TCJA: 100% Deductible*
  - o Also repeals employer deduction for employer-provided on premises meals and employer eating facilities after 2025
- Meals consumed on work travel remain 50% deductible

Net Operating Losses (C Corps)

- **Net Operating Losses (Pre-TCJA)**
  - 2 Year Carryback
  - 20 Year Carryforward
  - *AMT NOL – Offset 90% AMT Income*
- **Net Operating Losses (Under TCJA)**
  - Carryback *Repealed*
  - NOLs generated after 2017 – Carryforward offsets 80% taxable income in future years
  - Carried forward indefinitely
    - *Pre-2018 NOLS retain 20-year carryover restriction*

Accounting Methods

- **Cash Method of Accounting (Pre-TCJA)**
  - C corporations and partnerships with C corporations as a partner with gross receipts < $5M.
  - Small businesses with gross receipts < $1M
  - Certain industries with gross receipts < $10M
  - Inventory costs may not be deducted until sold
- **Cash Method of Accounting (Under TCJA)**
  - Permitted for all businesses with average annual gross receipts < $25M
  - Inventory accounted for as non-incidental supplies (i.e. hold cost until sold) or by conforming to method reflected on financial statements
  - *Automatic Consent Accounting Method Change*

Accounting Methods

- **UNICAP (Pre-TCJA)**
  - Manufacturers of inventory required to capitalize indirect costs
  - Resellers of inventory with gross receipts > $10M required to capitalize certain indirect costs
  - Applies to real property constructed by taxpayers
  - Businesses with average annual gross receipts < $10M exempt
- **UNICAP (Under TCJA)**
  - Gross receipts exemption test increased from $10M to $25M
  - *Automatic Consent Accounting Method Change*

Accounting Methods

- **Long-Term Contracts (Pre-TCJA)**
  - Generally, Percentage of Completion method required
  - Completed Contract method permitted for businesses with gross receipts < $10M or contracts expected to be completed within two years
- **Long-Term Contracts (Under TCJA)**
  - Gross receipts exemption test increased from $10M to $25M
  - *Automatic Consent Accounting Method Change*
  - *Conversion is done on a cut-off basis for new contracts*

Business Credits

- **Retained:**
  - Employer-Provided Child Care Credit
  - Research & Development Credit
  - 20% Credit for Rehab of Certified Historic Structure
  - Work Opportunity Tax Credit (WOTC)
  - New Markets Tax Credit
  - Investment in Qualified Community Development
  - Disabled Access Credit
  - Employer Tip Credit
- **Modified:**
  - Orphan Drug Credit – Modified from 50% to 25% of qualified clinical testing expenses
- **Repealed:**
  - 10% credit for qualified rehabilitation expenditures with respect to pre-1936 buildings

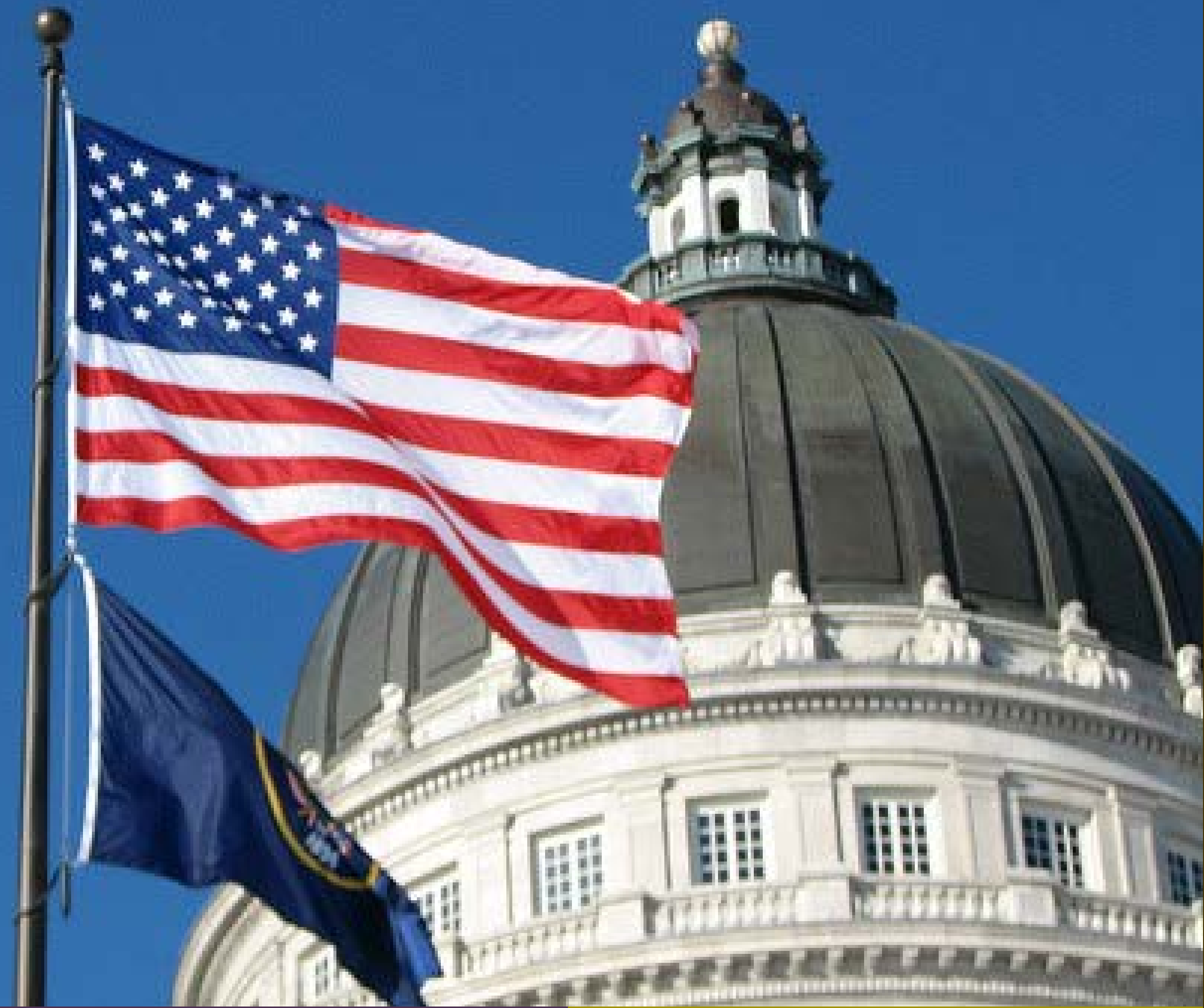
Business Credits

- **New Credit - Employer-Paid Family and Medical Leave:**
  - Credit = 12.5% wages paid to qualifying employees during any period in which employees are on family and medical leave
    - Rate of payment must be > 50% wages normally paid
    - Credit increased 0.25% for each percentage point by which payment rate exceeds 50%
    - Maximum credit = 25%
    - Maximum 12 Weeks
  - Not available to the extent that family and medical leave is mandated by state or local law
  - Eligible Employer – Requires written policy allowing all qualifying full-time employees not less than two weeks annual paid family and medical leave
  - Available for 2018 and 2019 Only
  - Allowed against AMT

Research Expenses

- **Research Expenses (Pre-TCJA)**
  - Deductible in the year incurred
- **Research Expenses (Under TCJA)**
  - "Specified R&E Expenses" must be capitalized and amortized over five years
    - Includes expenses for software development, exploration expenses related to oil & gas and other minerals
    - Not Included: Expenses for land or depreciable property used in connection with R&E
  - Effective for amounts paid or incurred in tax years beginning after 2021

Tax Cuts and Jobs Act (TCJA)



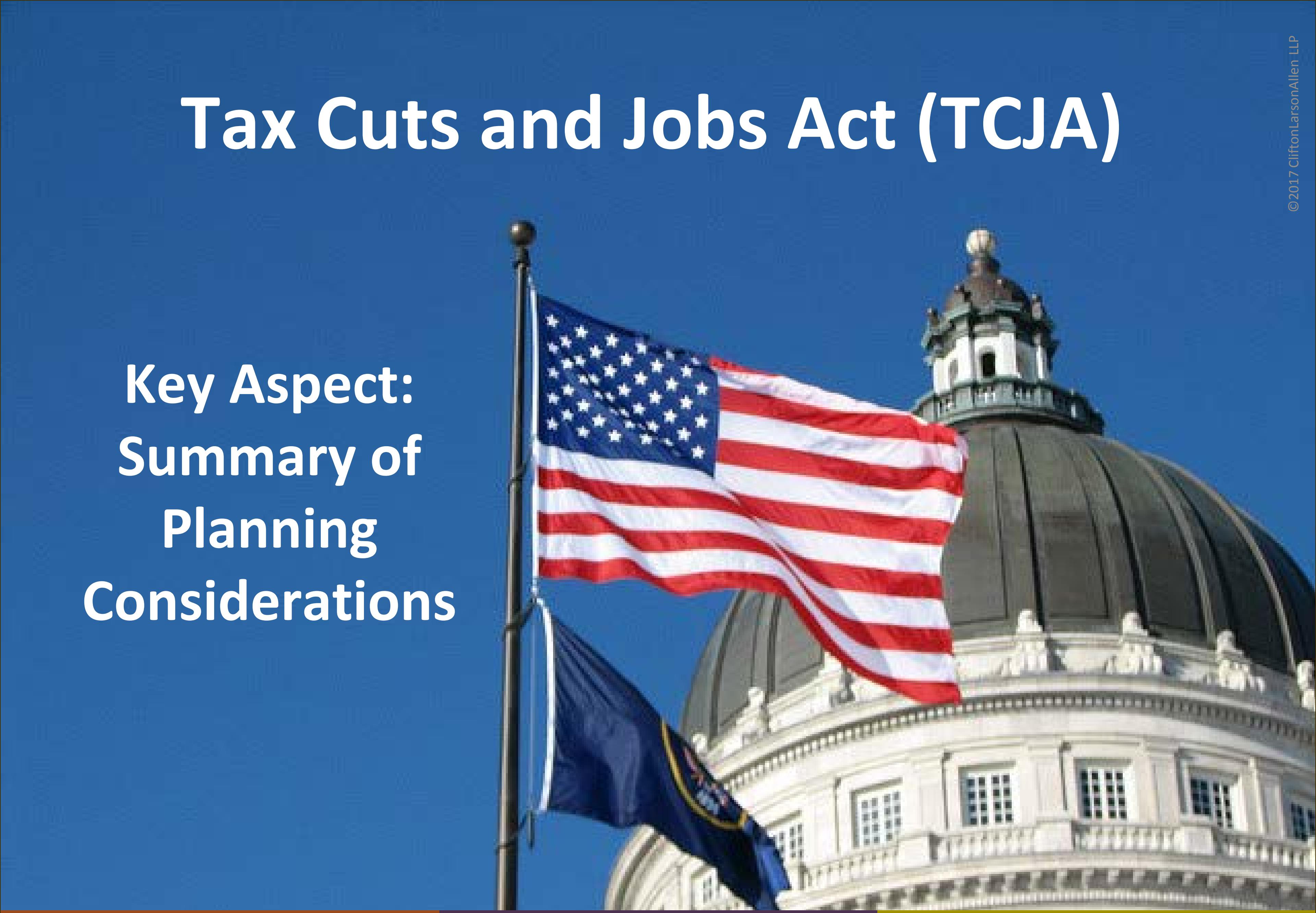
Key Aspect: Selected International Provisions

100 Percent DRD for Foreign Source Portion of Dividends

- **Foreign Source Portion of Dividends (Pre-TCJA): DRD**
  - FI earned by a FS of a U.S. corporation generally is not subject to U.S. tax until the income is distributed as a dividend to the U.S. corp.
- **Foreign Source Portion of Dividends (Under TCJA):**
  - Participation exemption - 100% dividend received deduction (DRD) for domestic C corporations
  - Applicable to dividends from specified 10% owned foreign corporations
  - Not applicable to dividends from PFICs unless they are CFCs
  - Holding period – 365 days
  - No credit or deduction for foreign taxes paid or accrued
  - Dividend is excluded from FSI and any properly allocable expenses are excluded from FSE
  - Hybrid dividends treated as subpart F with no DRD
  - Effective: For distributions made after December 31, 2017

Tax Cuts and Jobs Act (TCJA)

Key Aspect: Summary of Planning Considerations



Summary

- **Planning Considerations**:
  - Cost Segregation Study – 2017
  - Modeling C vs. S Status
  - Accounting Method Review
    - Accrual to Cash
    - Completed Contract
    - LIFO Methods
  - Earnings and Profits (“E&P”) study
  - Transfer pricing study
  - IC-DISC: Will the benefit get diminished because of the new pass-through deduction?

Questions?

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