

SUMMARY OF TAX CUTS AND JOBS ACT OF 2017

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On December 22nd, President Trump signed the Tax Cuts and Jobs Act of 2017, a \$1.5 trillion tax cut. At the heart of the plan, the most sweeping since 1986, is a cut in the corporate tax rate to 21% from 35%. This is expected to provide a stimulus to the U.S. economy as soon as next year. The tax plan also cuts individual tax rates and aims to simplify the tax code by eliminating some deductions, trimming others and doing away with personal exemptions.

SELECTED CHANGES PRIMARILY IMPACTING INDIVIDUALS

INDIVIDUAL INCOME TAX RATES (Effective for tax years beginning after 2017 and before 2026) -

Single Individuals

If Taxable Income Is:

Not over \$9,525
Over \$9,525 but not over \$38,700
Over \$38,700 but not over \$82,500
Over \$82,500 but not over \$157,500
Over \$157,500 but not over \$200,000
Over \$200,000 but not over \$500,000
Over \$500,000

Then Income Tax Equals:

10% of the taxable income
\$952.50 plus 12% of the excess over \$9,525
\$4,453.50 plus 22% of the excess over \$38,700
\$14,089.50 plus 24% of the excess over \$82,500
\$32,089.50 plus 32% of the excess over \$157,500
\$45,689.50 plus 35% of the excess over \$200,000
\$150,689.50 plus 37% of the excess over \$500,000

Married Individuals Filing Joint Returns and Surviving Spouses

If Taxable Income Is:

Not over \$19,050
Over \$19,050 but not over \$77,400
Over \$77,400 but not over \$165,000
Over \$165,000 but not over \$315,000
Over \$315,000 but not over \$400,000
Over \$400,000 but not over \$600,000
Over \$600,000

Then Income Tax Equals:

10% of the taxable income
\$1,905 plus 12% of the excess over \$19,050
\$8,907 plus 22% of the excess over \$77,400
\$28,179 plus 24% of the excess over \$165,000
\$64,179 plus 32% of the excess over \$315,000
\$91,379 plus 35% of the excess over \$400,000
\$161,379 plus 37% of the excess over \$600,000

Married Individuals Filing Separate Returns

If Taxable Income Is:

Not over \$9,525
Over \$9,525 but not over \$38,700
Over \$38,700 but not over \$82,500
Over \$82,500 but not over \$157,500

Then Income Tax Equals:

10% of the taxable income
\$952.50 plus 12% of the excess over \$9,525
\$4,453.50 plus 22% of the excess over \$38,700
\$14,089.50 plus 24% of the excess over \$82,500

Over \$157,500 but not over \$200,000	\$32,089.50 plus 32% of the excess over \$157,500
Over \$200,000 but not over \$300,000	\$45,689.50 plus 35% of the excess over \$200,000
Over \$300,000	\$80,689.50 plus 37% of the excess over \$300,000

Heads of Households

<u>If Taxable Income Is:</u>	<u>Then Income Tax Equals:</u>
Not over \$13,600	10% of the taxable income
Over \$13,600 but not over \$51,800	\$1,360 plus 12% of the excess over \$13,600
Over \$51,800 but not over \$82,500	\$5,944 plus 22% of the excess over \$51,800
Over \$82,500 but not over \$157,500	\$12,698 plus 24% of the excess over \$82,500
Over \$157,500 but not over \$200,000	\$30,698 plus 32% of the excess over \$157,500
Over \$200,000 but not over \$500,000	\$44,298 plus 35% of the excess over \$200,000
Over \$500,000	\$149,298 plus 37% of the excess over \$500,000

Estates and Trusts

<u>If Taxable Income Is:</u>	<u>Then Income Tax Equals:</u>
Not over \$2,550	10% of the taxable income
Over \$2,550 but not over \$9,150	\$255 plus 24% of the excess over \$2,550
Over \$9,150 but not over \$12,500	\$1,839 plus 35% of the excess over \$9,150
Over \$12,500	\$3,011.50 plus 37% of the excess over \$12,500

CAPITAL-GAIN AND QUALIFIED DIVIDEND RATES (Effective for tax years beginning after 2017 and before 2026) –

<u>Tax Rate</u>	<u>Taxable Income</u>				
	<u>Joint</u>	<u>MFS</u>	<u>HOH</u>	<u>Single</u>	<u>Estates & Trusts</u>
0% - Less Than	\$77,200	\$38,600	\$51,700	\$38,600	\$2,600
15% - At Least	\$77,200	\$38,600	\$51,700	\$38,600	\$2,600
Less Than	\$479,000	\$239,500	\$452,400	\$425,800	\$12,700
20% - More Than	\$478,999	\$239,499	\$452,399	\$425,799	\$12,699

“KIDDIE TAX” (Effective for tax years beginning after 2017 and before 2026) -

Unearned Income - Taxed under rate schedules for trusts and estates.

Earned Income - Taxed under rate schedules for single individuals.

Note: The child’s tax on unearned income is no longer taxed at the child’s parents’ rates. As under current law, the “Kiddie Tax” applies to a child if: **1)** the child **a)** has not reached the age of 18 by the close of the taxable year, **b)** is age 18 at the end of the year and does not have earned income of more than half the

child's support, or **c)** the child is at least age 19 and is a full-time student under the age of 24 and does not have earned income of more than half the child's support; **2)** either of the child's parents is alive at the end of the year; **3)** the child's unearned income exceeds \$2,100 (for 2018); **and 4)** the child does not file a joint return.

THE STANDARD DEDUCTION (Effective taxable years beginning after 2017 and before 2026) -

Amount of Standard Deduction:

<u>Joint Return</u>	<u>Single</u>	<u>Head of Household</u>
\$24,000	\$12,000	\$18,000

Note: The Act retains the additional standard for over age 65 and blind through 2025.

Dependents. The standard deduction of someone who is a dependent of another is limited to the **greater of 1)** \$1,050, or **2)** \$350 plus the individuals earned income for 2018 and this provision was not changed by the Act.

REPEAL OF DEDUCTION FOR PERSONAL EXEMPTIONS (Effective taxable years beginning after 2017 and before 2026) -

The Act repeals the personal exemption for taxable years beginning after 2017 and before 2026.

ENHANCEMENT OF CHILD TAX CREDIT AND NEW FAMILY TAX CREDIT (Effective tax years beginning after 2017 and before 2026) –

1. "Child Tax Credit" increased to \$2,000 for a **"Qualifying Child "< 17** (up from \$1,000 per child). **Must include a Social Security Number for each "qualifying child"** for whom the Child Tax Credit is claimed and the Social Security number must be issued before the due date for filing the return for the taxable year.

Note: Does not apply to a dependent other than a **"Qualifying Child."**

2. Nonrefundable credit of \$500 for each dependent **other than a "Qualifying Child."**

3. Phase out of combined credits (1 & 2 above) begins at \$400,000 for joint filers (currently \$110,000) and \$200,000 for single filers (currently \$75,000). These amounts are not indexed for inflation.

4. Limits the *Refundable* Child Credit to \$1,400 (rather than \$1,000).

SIMPLIFICATION AND REFORM OF EDUCATION INCENTIVES

MODIFICATION OF RULES FOR §529 PLANS –

1. May Distribute Up To \$10,000 For Elementary and High School Tuition (Effective for *distributions after 2017*).

The Act permits §529 plans to distribute up to \$10,000 for tuition incurred during a taxable year in connection with the enrollment or attendance of the designated beneficiary at a public, private or religious elementary or secondary school. This limitation applies on a per-student basis. Thus, an individual who is a designated **beneficiary of multiple §529 plans may receive total distributions during a taxable year of no more than \$10,000.** Any excess over this amount would be treated as distributions subject to tax under the general distribution rules for §529 plans.

2. May Roll Amounts From 529 Plan Into ABLE Account (Effective for distributions after date of enactment and before 2026). The Act allows distributions from a 529 plan to be rolled into an ABLE account without penalty, provided the ABLE account is owned by the designated beneficiary of that 529 account, or a member of such designated beneficiary's family. (ABLE accounts were established by the Achieving a Better Life Experience Act of 2014 to encourage individuals and families to provide private funding to assist disabled individuals in maintaining a healthy independent and quality life style.) **Amounts rolled over count towards the overall limitation** for contributions to the ABLE account for the year. Any amount rolled over in excess of the contribution limits for the year is includible in the gross income of the distributee.

DISCHARGE OF CERTAIN STUDENT LOAN INDEBTEDNESS ON ACCOUNT OF DEATH OR DISABILITY (Effective for discharges after 2017 and before 2026) –

1. Excluded From Income After 2017. Any income resulting from the *discharge of certain student debt* on account of the *death or total permanent disability* of the student is *excluded from taxable income for discharges after 2017*.

2. Loans Qualifying for Exclusion. Loans eligible for the exclusion under the Act are loans made by **1)** the United States (or an instrumentality or agency thereof), **2)** a State (or any political subdivision thereof), **3)** certain tax-exempt public benefit corporations that control a State, county, or municipal hospital and whose employees have been deemed to be public employees under State law, **4)** an educational organization that originally received the funds from which the loan was made from the United States, a State, or a tax-exempt public benefit corporation, and private education loans (for this purpose, private education loan is defined in section 140(7) of the Consumer Protection Act).

SIMPLIFICATION AND REFORM OF INDIVIDUAL DEDUCTIONS

REPEAL 3% OF AGI PHASE OUT OF ITEMIZED DEDUCTIONS (Effective for tax years after 2017 and before 2026) - The Act repeals the 3% of AGI phase-out rule as an individual's AGI exceeds certain thresholds.

REPEAL MISCELLANEOUS ITEMIZED DEDUCTIONS SUBJECT TO 2% SUBTRACTION (Effective for taxable years beginning after 2017 and before 2026) - The Act *repeals all "Miscellaneous Itemized Deductions"* that are currently subject to 2% of AGI subtraction effective for tax years beginning after 2017 and before 2026.

HOME MORTGAGE INTEREST - The Act generally retains the home mortgage interest deduction, with the following changes *effective for debt incurred after December 15, 2017*.

1. Limit For Home Acquisition Indebtedness. The Act *reduces* the **\$1 million limitation** for home *"Acquisition Indebtedness"* to **\$750,000** for *Acquisition Indebtedness incurred after December 15, 2017* (the limitation for *married individuals filing separate returns* would be reduced from \$500,000 to **\$375,000**).

2. Second Homes. Loans to purchase, construct, or improve second homes continue to qualify as home acquisition indebtedness as under current law.

3. Interest On Home Equity Indebtedness Not Allowed (Effective for tax years beginning after 2017 and before 2026). The Act provides that interest on home equity indebtedness would not be deductible for tax years beginning after 2017 and before 2026.

4. Refinancing Home Acquisition Indebtedness Incurred On Or Before December 15, 2017. For the *refinancing of debt incurred on or before December 15, 2017* the refinanced debt generally would be treated as incurred on the same date that the original debt was incurred for purposes of determining the limitation amount applicable to the refinanced debt. However, this refinancing rule does not apply after the expiration of the term of the original indebtedness or, if the principal of such original indebtedness is not amortized over its term, the expiration of the term of the first refinancing of such indebtedness (or if earlier, the date which is 30 years after the date of such first refinancing).

5. Pre-December 15, 2017 Binding Contract To Close Before 2018. In the case of a taxpayer who enters into a *written binding contract before December 15, 2017* to close on a residence *before 2018*, and who *purchases the residence before April 1, 2018*, the *\$1,000,000 limitation* on Home *Acquisition Indebtedness* applies to *Acquisition Indebtedness* incurred *before April 1, 2018*.

6. \$1,000,000 Limitation For Taxable Years Beginning After 2025. The Act provides that for taxable years beginning after 2025, the limitation on home acquisition indebtedness will revert to \$1,000,000.

ITEMIZED DEDUCTION FOR STATE AND LOCAL PROPERTY TAXES AND INCOME TAXES OR SALES TAXES IN LIEU OF INCOME TAXES LIMITED TO \$10,000 OR \$5,000 IF MARRIED FILING SEPARATE RETURNS (Effective for tax years beginning after 2017 and before 2026) –

1. \$10,000/\$5,000 Limit. The Act limits the itemized deduction for *State and local property taxes and income taxes* (or sales taxes in lieu of state and local income taxes) *to \$10,000* (\$5,000 for married individuals filing separate returns).

Note: Foreign real property taxes may not be deducted under this exception.

2. Property Taxes And Sales Taxes Incurred In Carrying on Trade or Business Are Deductible. The Act continues the deduction for *State and local property and*

sales taxes paid or accrued in **carrying on a trade or business** or producing income (i.e., **Schedules C, E, and F**).

3. Anti-Abuse Rule For 2017 Pre-Payment Of 2018 State And Local Income Taxes.

The Act provides that “*an amount paid in a taxable year beginning before January 1, 2018, with respect to a State or local income tax imposed for a taxable year beginning after December 31, 2017, shall be treated as paid on the last day of the taxable year for which such tax is so imposed.*” In addition, the Conference Committee explanation of the Act says, “*Thus, under this provision, an individual may not claim an itemized deduction in 2017 on a pre-payment of income tax for a future taxable year in order to avoid the dollar limitation applicable for taxable years beginning after 2017.*” **Note:** It is unclear whether this provision applies to overpayments of 2017 state income taxes as well as prepayments of 2018 taxes.

REPEAL OF DEDUCTION FOR PERSONAL CASUALTY AND THEFT LOSSES EXCEPT FOR PRESIDENTIALLY DECLARED DISASTER LOSSES (Effective tax years beginning after 2017 and before 2026)

- The Act *repeals the deduction* for *personal casualty losses and theft losses for tax years beginning after 2017 and before 2026*. However, the Act continues to allow a deduction as provided under current law for personal casualty losses attributable to a disaster declared by the President under §401 of the Robert T. Stafford Disaster Relief And Emergency Assistance Act.

LIMITATION ON GAMBLING LOSSES AND DEDUCTIONS (Effective for tax years beginning after 2017 and before 2026)

- The Act limits the deduction for gambling losses (i.e., wagering losses) *as well as any other deduction related to gambling* (e.g., travel expenses of a professional gambler and costs of wagers) *to gambling winnings*.

CHARITABLE CONTRIBUTIONS (Effective for contributions in tax years beginning after 2017)

- The Act retains the charitable contribution itemized deduction but makes several changes to the deduction, including:

- 1. 50% Of AGI Limit Increased To 60%.** The Act increases the 50% AGI limitation for cash contributions to public charities and certain other organizations to 60%.

2. **Repeal Of 80% Deduction Where Taxpayer Receives Right To Purchase Tickets To Athletic Events.** The Act denies a charitable contribution deduction for contributions made to colleges and universities in exchange for which the contributor receives the right to purchase tickets or seating at an athletic event.

DECREASE IN MEDICAL EXPENSE DEDUCTION SUBTRACTION FROM 10% TO 7½% (Effective for tax years beginning in 2017 and 2018) - The Act reduces the *medical deduction subtraction threshold to 7.5%* for all taxpayers for tax years beginning *in 2017* and 2018.

REPEAL DEDUCTION AND INCOME INCLUSION OR ALIMONY PAYMENTS (Generally effective for any divorce or separation instrument executed after 2018) - The Act *eliminates the deduction* for *alimony and separate maintenance* payments and such payments *would not be includible in the income of the payee*. This provision is *effective* for any *“Divorce or Separation Instrument”* *executed after 2018* and to any *Divorce or Separation Instrument* *executed before 2019 and modified after 2018* which provides that this repeal applies to the modification.

NO DEDUCTION FOR MOVING EXPENSES (Effective tax years beginning after 2017 and before 2026) - The Act **generally eliminates the deduction for moving expenses** for tax years beginning after 2017 and before 2026. However, the Act retains the deduction for moving expenses and the exclusion for reimbursements of these expenses for members of the Armed Forces on active duty who move pursuant to a military order because of a permanent change of station.

SIMPLIFICATION AND REFORM OF EXCLUSIONS AND TAXABLE COMPENSATION

SUSPENSION OF EXCLUSION FOR QUALIFIED BICYCLE COMMUTING REIMBURSEMENTS (Effective tax years beginning after 2017 and before 2026) - The Act suspends the \$20 per month exclusion from gross income and wages for qualified bicycle commuting reimbursements.

EMPLOYEE ACHIEVEMENT AWARDS LIMITED TO TANGIBLE PERSONAL PROPERTY (Effective for amounts paid or incurred after 2017) - The Act

essentially *codifies Reg. 1.274-8(c)(2)* limiting deductible and excludable *Employee Achievement Awards* to awards of “*tangible personal property.*” The Act provides that *Tangible Personal Property* shall ***not include*** cash, cash equivalents, gift cards, gift coupons or gift certificates (other than arrangements conferring only the right to select and receive tangible personal property from a limited array of such items pre-selected or pre-approved by the employer), or vacations, meals, lodging, tickets to theater or sporting events, stocks, bonds, other securities, and other similar items.

REPEAL EXCLUSION FOR QUALIFIED MOVING EXPENSE REIMBURSEMENTS (Effective tax years beginning after 2017 and before 2026) - The Act *repeals the exclusion* under §132(a)(6) for an *employer’s reimbursement of moving expenses.*

SIMPLIFICATION AND REFORM OF SAVINGS, PENSIONS, RETIREMENT

REPEAL RULE PERMITTING RECHARACTERIZATION OF ROTH IRA CONVERSIONS (Effective for tax years beginning after 2017) - The Act *prohibits recharacterizations* of the conversion of a traditional IRA to a Roth IRA. **Note:** This change prevents an individual from recharacterizing a conversion of a traditional IRA to a Roth IRA by October 15th of the following calendar year.

EXTENDED ROLLOVER PERIOD FOR THE ROLLOVER OF PLAN LOAN OFFSET AMOUNTS IN CERTAIN CASES (Effective tax years beginning after 2017) - Under the Act, employees whose plan terminates or who separate from employment while they have plan loans outstanding would have *until the due date for filing their tax return for that year, including extensions* (instead of the current 60 days), to contribute the loan balance to an IRA to avoid taxation on the loan amount.

ESTATE AND GENERATION-SKIPPING TRANSFER TAXES

CURRENT UNIFIED EXCLUSION AMOUNT AND GST EXEMPTION AMOUNT DOUBLED (Effective for individuals dying and generation-skipping transfers after 2017 and before 2026) - The Act increases the *Basic Unified Exclusion Amount* for gift & estate tax purposes and the generation-skipping exemption amount *to \$10,000,000 (as indexed for inflation [i.e., \$11,200,000 for 2018])*, effective for

decedents dying and gifts & generation-skipping transfers made after 2017. The current exclusion amount for 2018 is \$5,600,000.

ALTERNATIVE MINIMUM TAX REPEAL

1. REPEAL THE ALTERNATIVE MINIMUM TAX (AMT) FOR CORPORATIONS (Effective tax years beginning after 2017). The Act *repeals* the *corporate AMT* for tax years beginning after 2017.

2. PROVIDE REFUNDABLE CREDIT FOR CORPORATE AMT CREDIT CARRYOVERS. A corporation would be allowed a *refundable credit* for each of the **tax years beginning in 2018, 2019, and 2020** equal to **50 percent** of unused AMT credit carryovers to those respective years in excess of the regular tax for those years. A **refundable credit of 100% of the AMT credit carryovers to the tax year beginning in 2021** in excess of the regular tax for that year, would be allowed for that tax year.

3. CONTINUE INDIVIDUAL AMT WITH HIGHER AMT EXEMPTION AMOUNTS AND PHASEOUT THRESHOLDS (Effective Tax Years beginning after 2017 and before 2026) - The Act *continues* the *Alternative Minimum Tax (AMT)* for *Individuals*. However, the AMT *exemption amounts* and *phaseout thresholds* would be *increased* as follows:

	<u>AMT Exemption Amounts</u>		<u>AMT Exemption Phase-Out Beginning AMTI Thresholds</u>	
	<u>Pre-Act 2018</u>	<u>Act 2018</u>	<u>Pre-Act 2018</u>	<u>Act 2018</u>
Joint Filers	\$86,200	\$109,400	\$164,100	\$1,000,000
Single Returns & HOH	\$55,400	\$70,300	\$123,100	\$500,000
Married Filing Separately	\$43,100	\$ 54,700	\$ 82,050	\$500,000
Trusts and Estates	\$24,600	\$24,600	\$ 82,050	\$ 82,050

AFFORDABLE CARE ACT PROVISIONS

REPEAL SHARED RESPONSIBILITY PAYMENT FOR INDIVIDUALS (Effective for months beginning after 2018) – The Act reduces the individual responsibility payment for individuals under §5000A *to zero* effective for *months beginning after 2018*.

SELECTED CHANGES PRIMARILY IMPACTING BUSINESSES

REDUCTION IN CORPORATE TAX RATE (Effective tax years beginning after 2017)

- The Act provide a *flat 21% tax rate* for “*C*” corporations (including *Personal Service C Corporations* (PSCs)) for *tax years beginning after 2017*.

DIVIDENDS RECEIVED DEDUCTION. *After 2017*, the Act would reduce the *80% corporate Dividends Received Deduction* to *65%* and would reduce *the 70% dividends* received deduction *to 50%*.

DEDUCTION FOR PROPRIETORSHIPS, PARTNERSHIPS, S CORPORATIONS, TRUSTS, AND ESTATES OF UP TO 20% OF CERTAIN QUALIFIED INCOME (Effective for tax years beginning after 2017 and before 2026) –

1. General Rule. Under the Act, individuals, proprietorships, partnerships, S corporations, trusts and estates are generally allowed a “**20% Deduction**” for certain *qualified business income, qualified cooperative dividends, qualified REIT dividends, and qualified publicly-traded partnership income*. The amount of the overall deduction is based on three separate amounts determined under three separate formulas, that are ultimately added together to determine the amount of the overall deduction. More specifically, the overall deduction is the sum of the following:

- 1) The lesser of: a) 20% of “*Qualified Business Income,*” of each “*Qualified Trade or Business*” or b) the *W-2 wage and capital limitation* for each such trade or business; plus**
- 2) 20% of the aggregate *REIT dividends and qualified publicly traded partnership income* for the year. (Note: The **sum of the amounts in items 1) and 2)** are limited to **20% of the excess of the taxable income** for the**

year over the **sum of a) any net capital gain** under §1(h), **plus b) the total amount of qualified cooperative dividends of the taxpayer for the year); plus**
3) the lesser of a) 20% of qualified cooperative dividends, or b) taxable income reduced by net capital gain for the year.

Overall Limitation. The amounts allowed under 1), 2), and 3) above may **not in the aggregate exceed the taxpayer's taxable income for the year reduced by net capital gain.**

2. Not a "For AGI" Deduction. The 20% deduction is not allowed in computing AGI. The deduction reduces taxable income.

3. 20% Deduction Does Not Reduce Self-Employment (S/E) Income. The 20% deduction applies only for purposes of "**Chapter 1**" of the Internal Revenue Code. Since the S/E tax rules are contained in "**Chapter 2**," the 20% deduction **is not allowed for S/E Tax purposes.**

4. "Qualified Business Income." Domestic "**Qualified Business Income**" (QBI) means the net amount of domestic qualified items of income, gain, deduction, and loss with respect to the taxpayer's "**Qualified Trade or Businesses**" which are included or allowed in determining taxable income. A "**Qualified Trade Or Business**" means **any trade or business other than: 1) a "Specified Service Trade or Business"** (described below), or **2) the trade or business of performing services as an employee.** "**Qualified Business Income**" **would not include** investment income (e.g., dividends), investment interest income, short-term capital gains, long-term capital gains, income from annuities, commodities gains, foreign currency gains, etc. "**Domestic**" income includes items of income, deductions, etc. that are "**effectively connected with the conduct of a trade or business within the United States (within the meaning of §864(c)).**"

"Qualified Business Income" Excludes Certain Reasonable Compensation-Type Payments To The Owner. "**Qualified Business Income**" **does not include** any amount paid **by an S corporation** that is treated as **reasonable compensation** paid to the taxpayer claiming the 20% deduction. Similarly, "**Qualified Business Income**" **would not include** any amount allocated or distributed by a partnership **to a partner** who is **acting other than in** his or her capacity as a partner for

services, and **would not include** any amount that is a **guaranteed payment for services** actually rendered to or on behalf of a partnership.

5. Deduction Limitation Based On W-2 Wages And Capital If Taxable Income Greater Than \$315,000/\$157,500. The 20% deduction for each qualified trade or business is **limited based on an owner's allocable share of the W-2 wages and capital** of a partnership or S corporation **or the W-2 wages and capital of a proprietorship**. However, the W-2 wage and capital limitation **does not apply** to owners whose taxable income (computed without regard to the 20% deduction) **does not exceed \$315,000** if married and **filing jointly (\$157,500 for others)**. The application of the wage and capital limitation is phased-in as an owner's taxable income goes from \$315,001 to \$415,000 on a joint return (\$157,501 to \$207,500 for others).

6. W-2 Wages and Capital Limitations. The limitation on the 20% deduction is **greater of 1) 50% of the W-2 wages** paid with respect to the qualified trade or business, or **2) the sum of 25% of the W-2 wages** with respect to the qualified trade or business **plus 2.5% of the unadjusted basis**, immediately after acquisition, **of all "qualified property."**

W-2 Wages. "W-2 wages" of a partnership, S corporation, or sole proprietorship is the sum of wages subject to wage withholding and elective deferrals into a §401(k) plan or a SIMPLE plan paid by the business during the calendar year ending during the taxable year. Only W-2 wages that are "*properly allocable*" to the taxpayer's *Qualified Business Income* are included.

"Qualified Property." "Qualified Property" is **tangible depreciable property 1)** held by and available for use in the qualified trade or business **at the close of the taxable year, 2)** which is used in the production of qualified business income, **and 3)** for which the **depreciable period has not ended before the close of the taxable year**. The "**depreciable period**" means the period **beginning** on the **date the property is first placed-in-service** by the taxpayer and **ending on the later of 1)** the date **10 years after that date, or 2)** the **last day of the last full year in the applicable recovery period** that would apply to the property under Section 168 (without regard to the alternative depreciation system under §168(g)).

7. Special Rule For Owners Of “Specified Service Trade Or Business” Where Taxable Income Is \$415,000/\$207,500 Or Less. The 20% deduction would be allowed for a “*Specified Service Trade or Business*” only *for owners* whose taxable income (computed without regard to the 20% deduction) **does not exceed \$315,000** if married and **filing jointly (\$157,500 for others)**. The deduction is phased-out as an owner’s taxable income goes from \$315,001 to \$415,000 on a joint return (\$157,501 to \$207,500 for others).

Specified Service Trade Or Business. A “*Specified Service Trade or Business*” means any trade or business activity involving the performance of services in the fields of health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services, or any trade or business where the principal asset of such trade or business is the reputation or skill of one or more of its employees. A “*Specified Service Trade or Business*” also includes any trade or business involving the services of investing and investment management, trading, or dealing in securities (as defined in §475(c)(2)), partnership interests, or commodities (as defined in §475(e)(2)). **Note:** A “*Specified Service Trade or Business*” **does not include** the performance of **architectural or engineering** services.

8. Application To S Corporations And Partnerships. The determinations under this provision would be made at the shareholder level (with respect to S corporations) and at the partner level (with respect to partnerships) taking into account the owner’s “allocable share” of each item of the underlying entity.

9. Trusts and Estates. Trusts and estates are eligible for the 20% deduction. Rules similar to the rules under present-law §199 would apply for apportioning between fiduciaries and beneficiaries any W-2 wages and unadjusted basis of qualified property under the limitation based on W-2 wages and capital.

10. Tiered Pass-Through Entities. The Act directs Treasury to promulgate regulations addressing how these rules would be applied in the case of “*tiered entities.*”

COST RECOVERY

100% §168(k) DEPRECIATION DEDUCTION (Generally effective for qualified property acquired and placed-in-service after September 27, 2017 and before January 1, 2023 [with an additional year for certain qualified property]) -

The Act makes the following changes to the current 50% immediate write-off for qualified §168(k) property:

1. **100% 168(k) Deduction For Qualifying Property “Acquired And Placed-In-Service” After September 27, 2017 and before January 1, 2023.** For *qualifying property “acquired and placed-in-service” after September 27, 2017 and before January 1, 2023* (with an additional year for certain qualified property), taxpayers will generally be able to expense **100% (instead of 50%)** of the cost of qualified 168(k) property. The 100% deduction will begin to phase out for qualifying property placed-in-service **after 2022** as follows: **1)** during 2023 - 80%, **2)** during 2024 - 60%, **3)** during 2025 - 40%, **4)** during 2026 - 20%, and **5)** after 2026 - 0% (with an additional year for certain qualified property).

Qualifying 168(k) Property Acquired “Before” September 28, 2017 And Placed-In-Service “After” September 27, 2017. Qualifying property *“acquired before” September 28, 2017 and “placed-in-service after” September 27, 2017* is allowed only a **50% deduction** under 168(k) if placed-in-service **before 2018**. Such property placed-in-service **after 2017** is subject to the following 168(k) depreciation amounts: **1)** 2018 - 40%, **2)** 2019 - 30%, and **3)** after 2019 - 0% (with an additional year for certain qualified property).

2. **Effective Date.** These provisions are generally effective for qualifying property **a)** that is acquired after September 27, 2017, and **b)** is placed-in-service after such date. Property shall not be treated as acquired after the date on which a written binding contract is entered into for such acquisition.
3. **Increase In Depreciation Caps For Passenger Autos.** For *passenger vehicles placed-in-service after December 31, 2017 and before January 1, 2023*, the Act increases the regular §280F depreciation caps (without regard to the \$8,000 increase) as follows: **1st year - \$10,000; 2nd year - \$16,000; 3rd year - \$9,600; fourth and subsequent years - \$5,760.**

The Act generally retains the \$8,000 increase in the §280F first-year depreciation cap through 2022 for qualifying passenger vehicles *“acquired and placed-in-service” after September 27, 2017 and before January 1, 2023*. However, such passenger vehicles *“acquired”* by the taxpayer **before September 28, 2017**, and *“placed-in-service” after September 27, 2017*, are

subject to the existing phase-out schedule for the increased \$8,000 §280F depreciation, as follows: placed-in-service in 2018 - \$6,400; placed-in-service in 2019 - \$4,800; placed-in-service after 2019 - \$0.

4. **Computer And Peripheral Property.** The Act removes computer or peripheral equipment from the definition of listed property.

5. **Application To Used Property.** In addition to allowing the §168(k) deduction for new property (as under current law), under the Act, ***property would also generally be eligible*** for the 168(k) additional depreciation ***if it is the taxpayer's first use*** of the property. **Caution!** Used Property will not qualify for the §168(k) deduction if it is acquired in a manner described in §179(d)(2)(A), (B), or (C). For example, the used property generally will not qualify if: **1)** it is acquired from a person whose relationship to the person acquiring it would result in the disallowance of losses under Section 267 or 707(b), **2)** it is acquired by one component member of a controlled group from another component member of the same controlled group, **3)** the basis of the property is determined in whole or part by reference to the adjusted basis of such property in the hands of the person from whom acquired (e.g., received by gift or part-purchase/part gift), **or 4)** the basis of the property is determined under §1014 (e.g., received property through inheritance). Moreover, the basis of replacement property acquired in a like-kind exchange will not qualify to the extent the replacement property's basis is determined by the relinquished property's basis.

6. **Application To Certain Qualified Film And TV Costs.** The Act would add to qualifying 168(k) property the cost of certain qualified film, television and live theatrical productions, effective for productions placed-in-service after September 27, 2017 and before 2023.

7. **Real Property Trades Or Businesses.** Effective for ***property placed-in-service in tax years beginning after 2017***, the Act would require a ***"Real Property Trade or Business"*** that "elects out" of the interest expense deduction limitation

(discussed later in this summary) to use the alternative depreciation system (ADS) to depreciate its: **1)** "nonresidential real property," **2)** "residential rental property," and **3)** "qualified improvement property." Therefore, if a real estate

trade or business ***“elects out”*** of the interest expense deduction limitation, it appears the real estate business's ***“Qualified Improvement Property”*** would not qualify for the first-year 168(k) bonus depreciation because property required to be depreciated under ADS does not qualify as 168(k) property (§168(k)(2)(D)). ***“Real Property Trades Or Businesses”*** is defined in §469(c)(7)(C) as any real property development, redevelopment, construction, reconstruction, acquisition, conversion, rental, operation, management, leasing, or brokerage trade or business.

- 8. §168(k) Depreciation Deduction is Generally Not Allowed For Property Used In a Trade or Business That Has Floor Plan Financing Indebtedness (Effective for tax years beginning after 2017)** - The Section 168(k) depreciation deduction is not available for any property used in a trade or business that has had floor plan financing indebtedness **unless the taxpayer** is exempt from the interest deduction limitation because the business's **average gross receipts are \$25,000,000 or less.**

OTHER CHANGES TO DEPRECIATION RULES. Generally, effective for property placed-in-service after 2017, the Act:

1. Shortens the recovery period for machinery or equipment used in a farming business from 7 to 5 years. The Act also repeals the requirement that property used in a farming business use the 150% declining balance depreciation method.
2. Provides a recovery period for ***“Qualified Improvement Property”*** of **15 years.**
3. Provides a 20-year ADS recovery period for ***“Qualified Improvement Property.”***
4. Lowers the ADS recovery period to 30 years for ***“Residential Rental Property.”***
5. **Effective for property placed-in-service in tax years beginning after 2017,** requires a farming business electing out of the investment interest deduction limitation to use ADS to depreciate property with a recovery period of 10 years or more.
6. Eliminates the separate definitions of ***“Qualified Leasehold Improvement Property,” “Qualified Restaurant Property,”*** and ***“Qualified Retail***

Improvement Property” and replaces those properties with “Qualified Improvement Property.”

EXPANSION OF SECTION 179 EXPENSING - The Act makes the following changes to the Section 179 deduction:

1. **Increase In §179 Deduction Caps.** Effective for *tax years beginning after 2017*, the Act *increases the expensing limitation* under §179 to ***\$1,000,000*** (up from \$510,000 for 2017) and increases the *phase-out threshold* to ***\$2,500,000*** (up from \$2,030,000 for 2017). These caps are to be indexed for inflation after 2018. Also, the \$25,000 cap for SUVs remains, but will be indexed for inflation beginning in 2019.
2. **Section 179 “Qualified Real Property” Expanded.** Effective for *property placed-in-service in tax years beginning after 2017*, the Act eliminates from the term “*Qualified Real Property*” (QRP) and removes the references to “*Qualified Leasehold Improvement Property*,” “*Qualified Restaurant Property*,” or “*Qualified Retail Improvement Property*.” Instead, under §179(f), QRP includes “***Qualified Improvement Property***” (as defined in §168(e)(6)). In addition, QRP includes any of the following improvements to non-residential real property, *if placed-in-service after the building was first placed-in-service*: Roofs, Heating, Ventilation, and Air-Conditioning Property, Fire Protection and Alarm Systems, and Security Systems.
3. **Property Used In Connection With Furnishing Lodging.** The Act amends §179 to include depreciable tangible personal property used to furnish lodging or in connection with furnishing lodging.

SMALL BUSINESS ACCOUNTING METHOD REFORM AND SIMPLIFICATION (Generally effective for tax years beginning after 2017) - The Act makes the following changes to tax accounting methods:

1. **\$5 Million Average Gross Receipts Safe Harbor for “C” Corporations Increased To \$25 Million Under §448.** Section 448 generally requires C corporations (except for PSCs and farming businesses) to use the accrual method of accounting, even if inventories are not a material income-producing factor, if the C corporation’s average gross receipts for the three

prior years is more than \$5 million. The current *\$5 million average gross receipts safe harbor* for regular “C” corporations to use the cash method of accounting is **increased to \$25 million** and the requirement that such businesses satisfy the requirement for all prior years would be repealed (**Note:** The increased \$25 million threshold would also apply to farm C corporations and farm partnerships with C corporation partners). In addition, the average gross receipts test would be indexed to inflation. **Note:** The Act indicates that C corporations currently using the accrual method because of the \$5 million threshold, will be able to switch to the cash method using the automatic accounting method change procedures if their average gross receipts are \$25 million or less. IRS will need to issue these automatic accounting method change provisions.

2. Special Rules For Businesses With Average Gross Receipts Of \$25 Million Or Less.

May Use Cash Method Of Accounting. Businesses with *average gross receipts of \$25 million or less* would be permitted to use the cash method of accounting even if the business *has inventories*.

3. Definition Of “Average Gross Receipts.” For purposes of the above rules for corporations and other businesses discussed above, **“Average Gross Receipts”** is as defined under §448(c). Under §448(c), **“Average Gross Receipts”** generally means the **average gross receipts for the three taxable years preceding the current year.**

REFORM OF BUSINESS-RELATED EXCLUSIONS, DEDUCTIONS, ETC.

BUSINESS INTEREST DEDUCTION LIMITED (Effective for taxable years beginning after 2017) - Generally, under the Act, a business may not deduct interest expense for a taxable year in excess of **1) Interest income, Plus 2) 30 percent** of the **business’s adjusted taxable income, Plus 3) Floor plan financing interest.** Any **excess is carried over to subsequent years** for an unlimited number of years.

1. “Business Interest Income.” Business interest income means the amount of interest includible in the taxpayer’s gross income and allocable to a trade or business. Business interest income does not include investment income.

2. **“Adjusted Taxable Income.”** Generally, “adjusted taxable income” is defined as **taxable income without regard to 1) Any item of income, gain, deduction, or loss not properly allocable to a trade or business, 2) Any business interest income or expense, 3) Any net operating loss, 4) Any deduction for depreciation or amortization (for tax years beginning after 2017 and before 2022), and 5) Any 20% deduction allowed under §199A.**
3. **Exceptions.** The Act provides exceptions from the interest expense limitation for: **1) Businesses with average gross receipts of \$25million or less (with the exception of tax shelters), 2) Certain regulated public utilities, 3) Any “electing” real property trades or businesses (as defined in §469(c)(7)(C) - i.e., any real property development, redevelopment, construction, reconstruction, acquisition, conversion, rental, operation, management, leasing, or brokerage trade or business), and 4) Any “electing” farming business.**

“Electing Real Property Trade or Business.” An electing real property trade or business is a real property trade or business that makes an **“irrevocable election”** to not be subject to the business interest expense limitation. **If the election is made** the real property trade or business is **required to use the alternative depreciation method** for any **nonresidential real property, residential rental property, and qualified improvement property held by** the electing real property trade or business.

“Electing Farming Business.” An electing farming business includes a **§263A(e)(4) farming business that makes an irrevocable election** to not be subject to the business interest deduction limitation, **and trades or businesses of a §199A(g)(2) specified agricultural or horticultural cooperative** with respect to which a cooperative makes an **irrevocable election** to not be subject to the interest deduction limitation. If the election is made the farming business or cooperative is **required to use the alternative depreciation method** for any property with a recovery period of 10 years or more which is **held by** such electing farming business.

4. **“Floor Plan Financing Interest.”** Floor plan financing interest means interest paid or accrued on floor plan financing indebtedness.

“Floor Plan Financing Indebtedness.” Qualified floor plan financing indebtedness generally means indebtedness used to finance the acquisition of motor vehicles held for sale or lease and secured by the inventory so acquired. A “motor vehicle” means any self-propelled vehicle designed for transporting persons or property on a public street, highway, or road, a boat, and farm machinery.

MODIFICATION OF NOL DEDUCTION (Generally effective for losses incurred in tax years beginning after 2017) – The Act makes the following changes to the NOL deduction:

- 1. Elimination Of 20-Year Limitation On NOL Carryovers (Effective for NOLs arising in tax years beginning after 2017).** The Act repeals the limitation on the number of years to which an NOL could be carried forward for tax years beginning after 2017.
- 2. Generally, NOL Carrybacks Not Allowed (Effective for NOLs arising in tax years beginning after 2017).** Generally, NOLs could not be carried back for NOLs arising in tax years beginning after 2017.

2-Year Carryback Only for Certain Farm Losses. The Act allows a 2-year carryback of any net operating loss attributable to a farming business as defined in §263A(e)(4).

2-Year Carryback and 20-Year Carryforward for NOLs of Insurance Companies. A property and casualty insurance company (as defined in §816(a) other than a life insurance company) may carry an NOL back 2 years and forward for 20 years.

- 3. NOLs May Not Offset More Than 80% Of Taxable Income (Effective for losses arising in tax years beginning after 2017).** The NOLs arising in taxable years beginning after 2017 and carried to future years, may not offset more than 80% of taxable income before the NOL deduction. NOLs of property and casualty insurance companies are not subject to this 80% limitation.

§1031 LIKE-KIND EXCHANGES ALLOWED ONLY FOR REAL PROPERTY (Generally, effective for exchanges completed after 2017) - The Act allows §1031 like-kind

exchanges ***only with respect to real property*** that is not held primarily for sale. However, the Act would provide a ***transition rule*** allowing ***like-kind exchanges of personal property to be completed*** if the taxpayer has either ***disposed of the relinquished property*** or ***acquired the replacement property on or before December 31, 2017***.

REPEAL DEDUCTIONS FOR CERTAIN ENTERTAINMENT EXPENSES, TRANSPORTATION FRINGES, ON-PREMISES GYMS, ETC. (Generally Effective for amounts paid or incurred after 2017). The Act makes the following changes:

- 1. No Deduction For Entertainment, Amusement Or Recreation Activities, Membership Dues, Or Related Facilities (Effective for amounts paid or incurred after 2017).** No deductions are allowed with respect to **1) an activity generally considered to be entertainment, amusement or recreation, 2) membership dues** with respect to any club organized for business, pleasure, recreation or other social purposes, **or 3) a facility or portion of a facility** used in connection with any of the above. Therefore, the Act **repeals the exception** to the deduction disallowance **for entertainment, amusement, or recreation** that is **directly related to** (or, in certain cases, **associated with**) the active conduct of the taxpayer's trade or business (and the related rule applying a 50% limit to such deductions). **Note:** The deduction for 50% of food and beverage expenses associated with operating a trade or business generally would be retained (e.g., meals consumed by employees during away from home travel).
- 2. Applies 50% Limit To Meals Provided To Employees On Employer's Premises (Effective for amounts incurred and paid after 2017 and before 2026).** The Act applies the 50% limit to employer expenses associated with meals provided for the employer's convenience on, or near, the employer's business premises through an employer-operated facility that meets the requirements of a de minimis fringe.
- 3. Disallows Employer's Deduction For Meals Provided For Employer's Convenience on Employer's Premises (Effective for amounts paid or incurred after December 31, 2025).** The Act disallows employer deductions for expenses associated with meals provided for the employer's convenience on,

or near, the employer's business premises through an employer-operated facility that meets the requirements of a de minimis fringe.

- 4. Disallows Deductions For "Qualified Transportation Fringes."** The Act disallows deductions for expenses associated with providing any qualified transportation fringe to employees and, except for ensuring employee safety, disallows any expense incurred for providing transportation (or any payment or reimbursement) for commuting between the employee's residence and place of employment.

REPEAL OF TECHNICAL TERMINATION OF PARTNERSHIPS (Effective for partnership tax years beginning after 2017) - The Act repeals the partnership "*technical termination*" rule under §708(b)(1)(B). Therefore, a *partnership would be treated as continuing* even if *50% or more* of the total *capital and profits interests* of the partnership *are sold or exchanged*, and *new elections would not be required or permitted*.

FINAL COMMENTS

Please contact Kelly CPAs and Consultants, LLC (410-893-0560) if you would like to discuss how these tax changes may affect your situation. Tax law is constantly changing due to new legislation, cases, regulations, and IRS rulings. Kelly CPAs and Consultants, LLC closely monitors these changes. In addition, please call us before implementing any planning ideas discussed in this letter, or if you need additional information. **Note:** The information contained in this material should not be relied upon without an independent, professional analysis of how any of the items discussed may apply to a specific situation.

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