Shannon & Associates LLP

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TAX REFORM – 2018 CHANGES

The Tax Cuts and Jobs Act, H.R. 1, was signed into law by President Trump on December 22nd. It contains a large number of provisions that will affect both businesses and individual taxpayers on a level not seen in over 30 years. Except for a few changes, most provisions in the bill are effective in 2018.

BUSINESSES

- For tax years after 2017 and before 2026, individuals may be allowed to deduct 20% of "qualified business income" from a partnership, S corporation, or sole proprietorships."Qualified business income" would not include an S corporation shareholder's reasonable compensation, guaranteed payments, or certain payments to partners. Certain specified service businesses (such as law, accounting, medical and dental, performing arts and most other services businesses) may not get the full 20% deduction.
- Reduce the corporate tax rate to 21% (down from the current top rate of 35%). Progressive rates for businesses with taxable income below $100,000 no longer apply.
- NOLs – 2-year carryback is repealed. NOL deduction is limited to 80% of taxable income, and can be carried forward indefinitely.
- Cash method of accounting – allowed for entities with less than $25 million of gross revenue, as long as income and deductions are represented fairly. Entities under $25 million are also not required to account for inventories and are not subject to the UNICAP rules.

- Corporate AMT is repealed.
- Provides immediate write off of the full cost of new or used equipment.
- Section 179 expensing increased to $1 million with a phase-out threshold of $2.5 million.
- Sec 179 allowed for qualified non-residential improvements, including roofs, HVAC, security systems, ventilation, etc.
- Eliminate the Domestic Production Activities Deduction (DPAD).
- Retains the low-income housing credit and the research & development credit.
- To protect the U.S. tax base, tax the foreign profits of U.S. multinational corporations at a reduced rate and on a global basis.

Most small business owners are going to need to evaluate whether they should convert their business to a C corporation. Factors to consider:

- Is your business a personal service business? Law, accounting, medical, financial consultants and brokers, and many other businesses will not qualify for the lower C corporation rate.
- What is your 5 and 10 year business goals? If you are planning on selling your business in the next few years, converting will probably cost you more tax overall.
- C corporations pay corporate income tax with its tax return at the new lower tax rate.
- Owner compensation is still subject to ordinary tax rates on the individual income tax return.
- Stockholder dividends are subject to tax on the individual income tax return.

- Each dollar of C corporation earnings will potentially be subject to “double tax”.
- How do prior S corporation earnings (AAA) get taxed? There are special rules related to this, which should also be planned for accordingly.
- We have built a template to evaluate the option of converting your business to a C corporation. Please call us to discuss. Most businesses will need to switch by March 15, 2018 in order to be taxed as a C corporation for 2018.

INDIVIDUALS

- Keep the number of tax brackets at seven, but reduces the overall top rate. The new brackets are: 10%, 12%, 22%, 24%, 32%, 35%, and 37%.
- Increase the standard deduction to $24,000 for married taxpayers filing jointly, and $12,000 for single filers.
- Eliminate the personal exemption.
- Increase the child tax credit from $1,000 to $2,000, as well as an additional $500 credit for each parent as part of a consolidated family tax credit.
- Retain the deduction for student loan interest, but limits the education credits.
- Under the new law, mortgage interest on loans used to acquire a principal residence and a second home is only deductible on debt up to $750,000 (down from $1 million), starting with loans taken out in 2018. And there is no longer any deduction for interest on home equity loans, regardless of when the debt was incurred.
- The deduction for job-related moving expenses has been eliminated, except for certain military personnel. The exclusion from W-2 income is repealed.
- Starting in 2019, there is no longer a penalty for individuals who fail to obtain minimum essential health coverage.
- Largely limits itemized deductions such as state income and sales taxes, and property taxes at a total of $10,000 per year, but retains the home mortgage interest and charitable contribution deductions.
- The AMT has been retained for individuals by the new law but the exemption has been increased to $109,400 for joint filers ($54,700 for married taxpayers filing separately), and $70,300 for unmarried taxpayers. The exemption is phased out for taxpayers with alternative minimum taxable income over $1 million for joint filers, and over $500,000 for all others.
- The estate tax exemption would be doubled from the current $5,000,000 (adjusted for inflation) to $10,000,000 for years 2018 to 2025.

With so many changes looming, it is a good idea to be proactive and start planning for these changes that will affect you in 2018. Should you have any questions regarding these law changes or emerging details, we recommend that you contact your Shannon & Associates advisor.