2017 TAX CUTS AND JOBS ACT

The Tax Cuts and Jobs Act was signed by President Trump on December 22, 2017. The Act makes sweeping changes to the U.S. tax code and impacts most taxpayers; especially individuals and businesses.

Except as noted, the new law is effective starting in 2018, but expires after 2025. The following highlights some of the many changes included in the Act. We can help you with its immediate and long-term impact on your situation. Please feel free to call our office for guidance on the provisions that directly affect you.

What it Means for Individuals

Individuals are more impacted by the provisions of the act than any other class of taxpayer. With the reduction in effective tax rates and the elimination or modification of many deductions, exclusions and credits, individual taxpayers are going to have to navigate a different maze in making decisions to maximize their tax benefits and minimize their tax liability.

Tax Rates

The individual income tax rates are modified to include 10, 12, 22, 24, 32, 35 and 37 percent. For 2017, the tax rates include 10, 15, 25, 28, 33, 35 and 39.6 percent. Qualified dividend and capital gain rates remain unaffected by the Act.

Personal Exemptions & Standard Deduction

Effective in 2018, the deduction for personal exemptions is eliminated. Likewise, the standard deduction is increased to almost double its current amount. The standard deduction is raised to $24,000 for joint filers, $18,000 for head-of-household filers and $12,000 for all other individuals.

Alternative Minimum Tax

Alternative minimum tax has been retained but increases both the exemption and exemption phase-out levels.

Affordable Care Act

The individual shared responsibility payment will be reduced to $0 after 2018 for those with insufficient health insurance coverage.

Itemized Deductions

The loss of many itemized deductions will channel an even greater number of taxpayers to the standard deduction. There are new limits on mortgage debt for purposes of the mortgage interest deduction. Annual itemized deductions for all state and local taxes, including property taxes, is capped at $10,000. The threshold for medical expense deductions is lowered to 7.5 percent of adjusted gross income (AGI) for tax years 2017 and 2018. The percentage limitation on charitable contributions increases from 50% of AGI to 60%. Additionally, miscellaneous itemized deductions subject to the two percent floor have been repealed.

Child Tax Credit

After 2017, the child tax credit increases from $1,000 to $2,000 per qualifying child. Up to $1,400 of that amount per qualifying child is refundable. The credit is also modified to include a $500 nonrefundable credit for qualifying dependents other than qualifying children. Phaseout thresholds have been raised from $110,000 to $400,000 of adjusted gross income for joint filers.

Education

Section 529 qualified tuition plans are modified to allow for distributions to be made for elementary and secondary tuition. Distributions for elementary or secondary tuition are limited to no more than $10,000 incurred during the tax year in connection with the enrollment or attendance of the designated beneficiary. The limitation applies on a per-student basis, not a per-account basis.

Estate and Gift

The basic exclusion amount for purposes of federal estate and gift taxes and the exemption amount for purposes of the generation-skipping transfer (GST) tax is doubled from $5 million to $10 million, before adjustment for inflation, for the estates of decedents dying and gifts and generation-skipping transfers made after 2017.

Other Modifications

The Act makes modifications to many provisions not mentioned above, such as the repeal of alimony deductions and inclusions for divorce or separation instruments executed or modified after 2018, modification of the tax brackets, repeal of moving expense deductions and many other provisions.

What it Means for Businesses

For businesses, tax benefits include a reduction in the corporate tax rate, increase in the bonus depreciation allowance and an enhancement to the Code Sec. 179 expense. Owners of partnerships, S corporations and sole proprietorships are allowed a deduction as a percentage of qualified income of pass-through entities, subject to a number of limitations and qualifications. On the other hand, numerous business tax preferences are eliminated.

Credit for Employer Social Security and Medicare Taxes Paid on Tips

Also known as the "Tip Tax Credit" or "IRC 45 B Credit," The Act does not modify or eliminate any of its provisions. Qualified taxpayers can continue claiming this credit for 2018.

Work Opportunity Tax Credit

The Act does not modify or eliminate any provisions of this credit. Qualified taxpayers can continue claiming this credit for 2018.

Corporate Taxes

A reduced flat 21-percent corporate tax rate is permanent beginning in 2018. This rate also applies to personal service corporations (PSCs). In addition, the 80-percent and 70-percent dividends received deductions under current law are reduced to 65-percent and 50-percent, respectively. The Act also repeals the alternative minimum tax on corporations.

Bonus Depreciation

The bonus depreciation rate has fluctuated over the last 15 years, from as low as zero percent to as high as 100 percent. The Act increases the 50-percent bonus depreciation allowance to 100 percent. It also removes the requirement that the original use of qualified property must commence with the taxpayer, thus allowing bonus depreciation on the purchase of used property. Additionally, the bonus depreciation provisions are being retroactively applied to property acquired after September 27, 2017. Property acquired before that date are subject to the old rules.

Section 179 Expensing

The Act sets the Code Sec. 179 dollar limitation to expense capital asset acquisitions at $1 million and the investment limitation to phase out the expensing at $2.5 million. In addition, certain types of building improvements are now eligible, including: roofs, HVAC, fire protection or alarm systems and security systems.

Previously, restaurant buildings and improvements to the exterior as well as the interior of the restaurant building qualified for Sec. 179 expensing under the qualified real property category. Under the new law, a restaurant improvement (or improvement to any other type of building) must meet the definition of “qualified improvement property.” This means that only internal improvements to a restaurant building (now including roofs, HVAC property, fire protection and alarm systems, and security systems) will qualify for expensing.

Automobiles

The $25,000 maximum Code Sec. 179 deduction will still be available for vehicles between 6,000 and 14,000 lbs., such as a sport utility vehicle, a truck with an interior cargo bed length less than six feet or a van that seats fewer than 10 persons behind the driver’s seat, but will now be adjusted for inflation.

The first-year depreciation cap on a passenger vehicle that is subject to the annual "luxury auto" depreciation limitations is increased by $8,000 if 100-percent bonus depreciation is claimed.

Deductions and Credits

Numerous business tax preferences are eliminated. These include the Code Sec. 199 domestic production activities deduction, non-real property like-kind exchanges and more. Additionally, the rules for business meals are revised, as are the rules for the rehabilitation credit. The research and development credit remains in place, but requires five-year amortization of research and development expenditures. The Act also creates a credit for employers paying employees who are on family and medical leave.

Interest Deductions

In an attempt to "level the playing field" between businesses that capitalize through equity and those that borrow, the Act generally caps the deduction for net interest expenses at 30 percent of adjusted taxable income, among other criteria. Exceptions exist for small businesses, including an exemption for businesses with average gross receipts of $25 million or less.

Pass-Through Businesses

Currently, up to the end of 2017, owners of partnerships, S corporations and sole proprietorships – also known as "pass-through" entities – pay tax at the individual rates, with the highest rate at 39.6 percent. Beginning in 2018, the Act allows a deduction in an amount equal to 20 percent of qualified business income of pass-through entities, subject to a number of limitations and qualifications.

If the owner's taxable income exceeds $157,500 for single filers or $315,000 for joint filers, the deduction is generally limited to the greater of (1) 50 percent of W-2 wages paid by the business, or (2) the sum of 25 percent of the W-2 wages paid plus 2.5 percent of the unadjusted basis of certain property the business uses to produce qualified business income. If the applicable item (1) or (2) is greater than 20 percent of qualified business income then this limitation does not apply.

Net Operating Losses

Net operating losses (NOLs) generated in tax years beginning after December 31, 2017 will be limited to 80 percent of taxable income. The Act also denies the carryback for NOLs in most cases while providing for an indefinite carryforward, subject to the percentage limitation.

Excess Business Losses for Noncorporate Taxpayers

Excess business losses of noncorporate taxpayers are not allowed for tax years beginning in 2018. An excess business loss is the excess of the taxpayer’s aggregate deductions for the tax year from the taxpayer’s trades or businesses, over the sum of the taxpayer’s aggregate gross income or gain for the tax year from such trades or businesses, plus $250,000 ($500,000 in the case of a joint return). Any disallowed excess business loss is treated as a net operating loss carryover to the following tax year.

Meals and Entertainment

The provision that (prior to 2018) allowed deductions for entertainment expenses is eliminated. Therefore, entertainment expenses paid or incurred after 2017, including expenses for a facility used in connection with entertainment such as sporting tickets and other entertainment events, generally are no longer deductible even if given to customers or employees.

Qualified business meals continue to remain 50% deductible in 2018 and subsequent years. Changes to meals deductions include (1) meals provided to employees on the employer's premises for the convenience of the employer and (2) meals provided to employees as de minimis fringe benefits. After December 31, 2025, these costs become nondeductible.

Since meals and certain entertainment expenses are now treated differently for purposes of deductibility, it is recommended to begin tracking meals and entertainment in separate general ledger accounts. Please let us know if you have any questions on how to implement this into your accounting system.

Some entertainment-related rules do not change. As under current law, club dues and membership costs are not deductible. Some entertainment expenses also remain fully deductible, including: (a) certain entertainment expenses for goods, services and facilities that are treated as compensation to an employee-recipient; (b) expenses for recreational, social or similar activities and related facilities primarily for the benefit of employees who are not highly compensated employees (such as holiday parties); (c) expenses for entertainment sold to customers; and (d) entertainment expenses for goods, services and facilities that are includible in the gross income of a non-employee recipient as compensation for services rendered or as a prize or award.

Transportation

Employers can no longer deduct expenses for transportation fringe benefits, except as necessary to ensure an employee's safety. These transportation fringe benefits include payments or reimbursements for van pools, transit passes and qualified parking expenses, unless treated as compensation income to the employee.

If you have questions regarding any provisions, including those not covered, please feel free to call our office.