

2018 Federal Tax Update: What we know.....for now....

December 5, 2017



Presenter

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Agenda

- House Plan
 - Individual impacts
 - Business impacts
- Hatch (Senate) Plan
- Differences between proposals
- General planning considerations
- Summary/Final thoughts

How I feel about taxes



How everyone else feels about taxes



House Proposal

- General overview and thoughts
 - November 2, 2017 House Republicans unveiled major overhaul of the Internal Revenue Code
 - Tax Cut and Jobs Act (TCJA)
 - White House has signaled support of House GOP bill
 - Impacts would be felt by both individuals and businesses
 - Have not seen this level of change in 30 years
 - There would be "winners" and there would be "losers"
 - Bill adds to the deficit
 - Several roadblocks along the way

House Proposal

So what are some general impacts?

- Year end planning for 2017 uncertainty?
 - 3 Possible outcomes
 - Final before year end
 - Early in 2018
 - Failing to move forward at all
 - » Timeline for conference and approval unknown
 - » Senate has their own tax bill and House has theirs
 - » Strong opposition by democrats
 - » Lobbying efforts to preserve certain tax breaks
- All indications to 2018 and beyond at this point

House Proposal

So what specific impacts can we expect?

- Lowering of the individual and corporate tax rates
- Repealing a significant number of tax credits and deductions
- Eliminating the Alternative Minimum tax
- Eliminating federal estate tax after 2023
- Enhancing child tax credit
- Business expensing. More generous.
- Increase to standard deduction for individuals
- And much, much more.....

Individual Impacts

Rate Bracket Squish and % changes

- 12, 25, 35, 39.6% - Plus 6% bubble tax on income \$1M-1.2M
- v.s. 10, 15, 25, 28, 33, 35, 39.6%

Rate	Joint Return	Individual Return
12%	\$0 - \$90,000	\$0 - \$45,000
25%	\$90,000 - \$260,000	\$45,000 - \$200,000
35%	\$260K - \$1M	\$200K - \$500K
39.6%	Over \$1M	Over \$500K

- Benefit of the 12% rate would be phased out for taxpayers in the 39.6% bracket
- 0.9% Medicare tax remains

Individual Impacts

Itemized vs. standard deduction

- Nearly doubling the standard deduction
 - MFJ = \$24,000
 - HOH=\$18,000
 - Single=\$12,000
- Goal is to simplify tax filing by cutting certain taxpayers who would otherwise do better itemizing deductions

Remove personal exemptions

- A tradeoff for higher standard deductions and better child tax credit

Individual Impacts

Deductions and Credits set for elimination

- State and local income and sales tax, teacher's classroom expenses, moving expenses, alimony, student loan interest, personal casualty losses and medical expenses and.....
 - What does this mean and who does it effect?
 - It funnels a large number of individuals to the standard deduction
 - Could have a broad impact on state and local governments, charitable organizations, real estate prices and individuals in general that rely on these

Home mortgage interest/state and local property tax

- \$1M → \$500K cap on mortgage interest
- \$10,000 cap on state and local property tax

Individual Impacts

Removing employee business expense

- Mileage, internet, cell phone etc.

No more AMT

Marriage penalty – For better, for worse?

- Example

No change to tax treatment of capital gains and qualified dividends

Marriage Penalty Example

Marriage Penalty Illustration - Assumes using standard deduction now					
2016 Tax Law			Proposed Law		
MFJ, one spouse with 200,000 of income, one spouse with 30,000 of income		Single, one person with income of 200,000 of income, one person with 30,000 of income	MFJ, one spouse with 200,000 of income, one spouse with 30,000 of income		Single, one person with income of 200,000 of income, one person with 30,000 of income
AGI	\$230,000	\$200,000	\$30,000	AGI	\$230,000
Standard Deduction	(\$12,600)	(\$6,300)	(\$6,300)	Standard Deduction	(\$24,400)
Personal Exemptions	(\$8,100)	(\$4,050)	(\$4,050)	Personal Exemptions	\$0
Taxable Income	\$209,300	\$189,650	\$19,650	Taxable Income	\$205,600
Tax	\$45,690	\$46,139	\$2,488	Tax	\$39,700
Total	\$45,690	\$48,627		Total	\$39,700
Savings of \$3037			Savings of \$9,316		
Cost of 2012					
MFJ, one spouse with 200,000 of income, one spouse with 30,000 of income		Single, each person has \$115,000 of income	MFJ, one spouse with 200,000 of income, one spouse with 30,000 of income		Single, each person has \$115,000 of income
AGI	\$230,000	\$115,000	\$115,000	AGI	\$230,000
Standard Deduction	(\$12,600)	(\$6,300)	(\$6,300)	Standard Deduction	(\$24,400)
Personal Exemptions	(\$8,100)	(\$4,050)	(\$4,050)	Personal Exemptions	\$0
Taxable Income	\$209,300	\$104,650	\$104,650	Taxable Income	\$205,600
Tax	\$45,690	\$22,339	\$22,339	Tax	\$39,700
Total	\$45,690	\$44,678		Total	\$39,700
Savings of \$6,100			Savings of \$6,100		

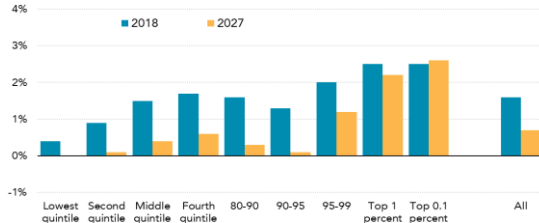
Individual Impacts

- “Corporate Greed” provisions
 - \$1M W-2 cap repeal for certain company executives (deductibility)
 - Pease limitation repealed = No Phase-out of itemized
- Currently no repeal of the Affordable Care Act taxes
 - Net investment income tax
 - Additional Medicare tax
 - But Senate??



Individuals

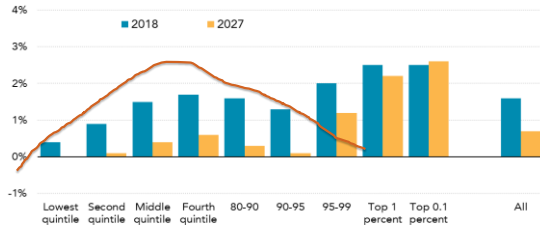
FIGURE 1
Percent Change in After-tax Income of the "Tax Cuts and Jobs Act"
By expanded cash income percentile, 2018 and 2027



Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0217-1).

Individuals

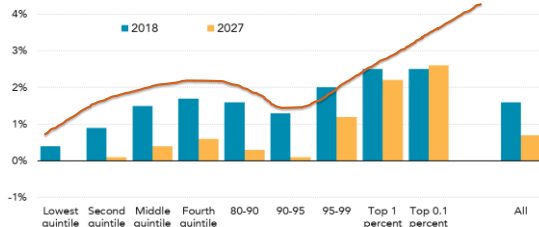
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Individuals

Distribution of Federal Tax Change of the "Tax Cuts and Jobs Act"
By expanded cash income percentile, 2018*



Expanded cash income percentile ^a	Percent change in after-tax income ^b	Share of total federal tax change (%)	Average federal tax change (dollars)	Average federal tax rate ^c	
				Change (% points)	Under the proposal (%)
Lowest quintile	0.4	1.3	-60	-0.4	3.7
Second quintile	0.9	5.8	-310	-0.9	7.8
Middle quintile	1.5	13.9	-840	-1.3	12.6
Fourth quintile	1.7	22.1	-1,590	-1.4	15.9
Top quintile	1.9	56.6	-4,840	-1.4	24.1
All	1.6	100.0	-1,180	-1.3	18.5
Addendum					
80-90	1.6	13.0	-2,300	-1.3	18.9
90-95	1.3	7.4	-2,570	-1.0	21.0
95-99	2.0	14.8	-6,600	-1.5	23.7
Top 1 percent	2.5	20.6	-37,440	-1.7	30.9
Top 0.1 percent	2.5	10.0	-178,560	-1.7	31.7

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0217-1).

Business Impacts

- 📌 Decrease in corporate tax rates
 - 35% to 20%
 - Many businesses currently pay an effective tax rate that is considerably less anyway

📌 Pass-through changes

- 39.6% top rate taxed at individual level to 25% tax for pass through qualified business income (70/30 split)
 - 70/30 – actively involved, 70% taxed at regular and 30% taxed at lower rates
 - Exception for less than \$75K in taxable income – 9%

Business Impacts

📌 Ohio BID treatments comes to fed passthrough

- Ohio breaks all income into 2 categories: Business and Non-business income.
- “Business income” is given lower rate
- “Non-business income” is taxed at normal rates
- Games/incentive to convert non-business income to business income --- harvest lower rate due to structural change.

Business Impacts

📌 Cap interest expense

- 📌 Cap deduction at 30% of adjusted taxable income
 - Exception for “small businesses” (who can still get 100%)

📌 Depreciation changes

- Bonus depreciation has varied significantly over the last several years
- Some believe that bonus depreciation doesn’t necessarily motivate it only incentivizes businesses to accelerate planned purchases, therefore.....
 - 100% immediate expensing of qualified property for a 5 year period
 - Increase Sec. 179 expensing to \$5M

Business Impacts

📌 Elimination of Sec 199 domestic production activities , non real property like-kind exchange, Work opportunity tax credit.

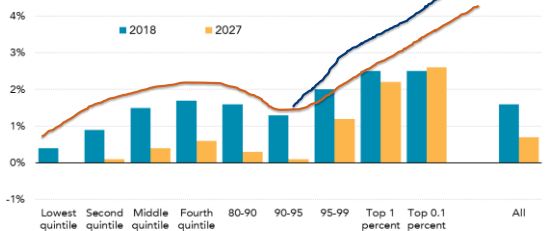
- 📌 Geothermal appears to be included in House proposal
- 📌 Business meals would be revised, along with net operating losses.
- 📌 Like-kind exchanges would only be allowed for real property.
 - Currently is for a wide range of property held for productive use or investment
- 📌 NOL use limited to 90% of taxable income and carried forward indefinitely

The Hatch (Senate) Plan

- 📌 Cut the corporate tax rate from 35 percent to 20 percent, but not until 2019.
- 📌 Cut taxes on pass-through businesses by allowing them a 23% percent deduction for qualified domestic income
- 📌 Retain seven individual income tax rates, with a top rate of 38.5 percent.
- 📌 Raise the standard deduction to \$12,000 for individuals and \$24,000 for married couples but repeal personal exemptions.

Individuals

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Percent Change in After-tax Income of the “Tax Cuts and Jobs Act”
By expanded cash income percentile, 2018 and 2027



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The Hatch (Senate) Plan

- 🕒 Increase the child tax credit from \$1,000 to \$2,000 and make it available for 17-year-olds and for families making as much as \$1 million. It would also create a new \$500 credit for other dependents.
- 🕒 Repeal the Alternative Minimum Tax. Now they have left some portion of this in, but seems undefined at this point
- 🕒 Roughly double the estate tax exemption but retain the tax. Would go to \$11mil
- 🕒 Repeal the deductions for state and local income, sales, and property taxes but keep deductions for mortgage interest, charitable giving, and medical expenses.

The Hatch (Senate) Plan

- 🕒 Index tax rates and other provisions using the chained CPI method that is less generous than the inflation index used currently.
- 🕒 A recent change is the repeal of the Affordable Care Act's tax penalties for those who do not have health insurance—pay or play mandate.

The Hatch (Senate) Plan vs. The House Plan

- 🕒 Very similar at a high level but there are differences!
 - Differences
 - Scrap entire SALT/property tax deduction vs. retain limited deduction for property taxes
 - Leave mortgage interest alone (except for home equity loans) vs. caps on the mortgage interest deduction
 - Retain medical expense deduction vs. repeal
 - Pass-throughs
 - Top rate of 32% vs. 25% and an additional low rate for business owners making less than \$75,000
 - ACA individual mandate repeal vs. no mention of repeal
 - Senate has different chamber rules. Cannot drive up long-term deficit if passed with 51 votes instead of 60.
 - Certain individual tax provisions terminated by 2026.

Planning in an Uncertain Environment

- 🕒 Stay flexible
- 🕒 Look at what has changed in your life, in your business
- 🕒 Be prepared
- 🕒 Don't get locked into a particular course of action
- 🕒 Focus on current tax law and optimize tax planning
- 🕒 Be wary of acting on planning opportunities based on proposed reform
- 🕒 View transactions with regard to both their economic and tax implications
- 🕒 Review your tax situation with a trusted advisor regularly

Planning in an Uncertain Environment

- 🕒 Small business owners especially need to monitor changes closely
 - Business credits and deductions. Extenders
- 🕒 Partnership agreements
 - Audits of partnerships in 2018 will see changes to rules governing the liability of each partner
 - Amend partnership agreements?

General Planning Considerations

- 🕒 Timing strategies and methods
 - Cash vs. Accrual method tax payer?
 - Cash method allows for some flexibility and control
 - Income acceleration/deferral
 - Sell or hold appreciated assets
 - Accelerate or delay bonuses
 - Manage year end bills and receipts
 - Declare special dividend
 - Like-kind exchange treatment
 - Deduction acceleration/deferral
 - Itemize 2017/standard deduction 2018
 - Contribute to retirement plans
 - Pay with check or credit card at year end
 - Pay estimated payments before year end

Summary

- 🕒 Plans seem to benefit higher income tier more than middle or lower tier (see graph and winner/loser throughout)
- 🕒 Inside each provision, there will be people that are hurt worse (see Ohio, NY, CA loss of SALT deduction) (lots of kids)
- 🕒 Not a spending cut, so we are either adding to deficit or moving around who pays
- 🕒 2017 is set, for year end planning include uncertainty in calculus of things hitting end of year 2017 vs 2018. (pre pay RE property tax). If with cash, wait to buy fixed assets. If debt, buy now b/c maybe grandfathered in.

Summary

- 🕒 So what do the votes look like??
 - 2 republican Senators indicated they will vote NO
 - Others have expressed a NO vote
 - Special election coming mid-December
 - May flip current republican seat to democrat
- 🕒 Bottom line....time is ticking to get this passed!

Questions?

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