

Tax Cuts and Jobs Act: Tax Reform 2017

Selected Items for Discussion

Guido van der Hoeven, EA
Extension Specialist / Sr. Lecturer
Dept. Agricultural and Resource Economics
NC State University

HMMMM.....

The difference between death and taxes is death doesn't get worse every time Congress meets.

-- Will Rogers



“Tax Cuts and Jobs Act”

- December 22, 2017, President Trump signed H.R. 1, the “Tax Cuts and Jobs Act” into law which now changes the taxation landscape for individuals and businesses.
- The digesting of what it all means has begun.
- Talk topics: Overview of changes:
 - Individual
 - Business

Individual Changes

- Tax rates have changed:
 - 2017: 10%, 15%, 25%, 28%, 33%, 35%, and 39.6%
 - 2018: 10%, 12%, 22%, 24%, 32%, 35%, and 37%
- Rate changes are effective for tax years beginning after December 31, 2017 and before January 1, 2026
- Estates and Trusts: 10%, 24%, 35% and 37%
 - At \$12,500 of taxable income goes to 37%

Individual Changes

- Standard Deduction increased for tax years beginning after December 31, 2017 and before January 1, 2026
 - MFJ \$24,000
 - Head-of-Household \$18,000
 - Single / MFS \$12,000
 - No changes to additional deduction amount for elderly or blind (\$1,050 or \$1,550 dependent upon filing status)

Individual Changes

- Personal Exemptions are **SUSPENDED**
 - For Tax years beginning after December 31, 2017 and before January 1, 2026.
 - Effectively reduces the exemption amount to zero.

Better off Tax wise?

- It depends!! A family with two kids, all things equal may have a higher tax liability:
 - Old rules: 2018 Standard Deduction MFJ \$13,000 plus 4 X \$4,150 = \$29,600 Tax Free Income
 - New rules: 2018 Standard deduction only: \$24,000 Tax Free Income

Individual Changes

- New measure of inflation index: now to use “chained CPI-U”
- Chained CPI-U generally grows at a slower pace because it takes into consideration that consumers substitute between goods in response to relative prices.

Individual Changes

- Kiddie Tax Modified:
 - Beginning for tax years after December 31, 2017 taxable earned income is taxed at single individual rates; and
 - Taxable income that is derived from unearned sources (portfolio, capital gains, etc.) are taxed according to estate and trust income tax brackets.
 - Estates and Trusts: 10%, 24%, 35% and 37%
 - At \$12,500 of taxable income goes to 37%

Individual Changes

- Capital Gains rates are retained:
 - 0%, 15%, and 20%
 - The new law maintains the breakpoints of the old law, but uses the chained CPI-U indexing for inflation for tax years after December 31, 2017.
 - 2018: 15% breakpoint is \$77,200 MFJ
20% breakpoint is \$479,000 MFJ

Individual Changes

- Income from Pass-Through Entities
 - For tax years beginning after December 31, 2017 and before January 1, 2026 a new deduction is added.
 - Sec. 199A “Qualified Business Income” (QBI), includes an estate and trust, from PTR, S-corp, LLC, sole proprietor is allowed to generally deduct 20% of QBI (farm profit) subject to W-2 wage limitations, except for sole proprietors, the greater of
 - 50% of W-2 wages with respect to the QBI
 - 25% of W-2 wages plus 2.5% of unadjusted basis of “qualified property” acquired in the tax year.

Individual Changes

- Net Operating Losses (NOLs)
- For tax years beginning after December 31, 2017 and before January 1, 2026,
 - 80% of losses allowed
 - Excess farm losses (\$300,000) regarding USDA subsidies no longer applies.
 - However, the NOL is generally not allowed in the year of the loss, but rather, is carried forward to subsequent tax years.

Individual Changes

- Personal Casualty and Theft Losses
- For tax years beginning after December 31, 2017 and before January 1, 2026,
 - Are suspended, except for personal casualty losses incurred in a Federally-declared disaster.

Individual Changes

- Child Tax Credit
 - New law increases to \$2,000 from \$1,000 for each qualifying child under 17 years of age.
 - AGI phase outs apply
 - Refundable amount increased to \$1,400 per qualifying child
 - SSN required for each child
 - Non-child dependent was added under the new law for an amount of \$500.

Individual Changes

- Itemized Deduction Changes for tax years beginning after December 31, 2017 and before January 1, 2026:
 - A Taxpayer may deduct State, Local and foreign property taxes, and State and local income taxes to a cap of \$10,000 or \$5,000 (MFS)
 - Mortgage Interest is allowed subject to indebtedness limitations \$750,000 (\$375,000 MFS)
 - Home equity mortgage interest deduction is suspended.

Individual Changes

- Charitable Contribution Deduction Limitation Increased
 - Beginning for tax years after December 31, 2017 and before January 1, 2026, the contribution limit is increased to 60%.
 - Example: AGI = \$100,000, limit is now \$60,000, any carry over of excess contributions can be carried forward five years.

The rule for contemporaneous written acknowledgment (CWA) has been repealed for tax years beginning after December 31, 2016.

Suspended Deductions

- Alimony Deduction after December 31, 2018
- Miscellaneous Itemized Deductions (2% floor)
- Qualified Bicycle Commuting Exclusion
- Moving Expense Reimbursements
- “Pease” Limitations on Itemized Deductions
- Moving Expenses Deduction
- Living Expenses of Members of CONGRESS

Repeal of OBAMACARE Individual Mandate after
12/31/2018

Estate and Gift Tax

- Gift Tax Exclusion Amounts for tax years beginning after December 31, 2017 and before January 1, 2026:
 - Annual Exclusion \$15,000
 - Lifetime Exclusion: \$11.2 million (\$22.4 per married couple)
- Step-up to FMV is retained
- Estate Exclusion Amount for tax years beginning after December 31, 2017 and before January 1, 2026:
 - \$11.2 million (\$22.4 per married couple)

Tax Reform Implications for Businesses

- C-corporation Changes
 - Flat tax at 21% (for those in 15% an increase of 40%)
 - Dividends-received deduction percentage decreased to 65% from 80%
 - Corporate AMT is repealed for tax years beginning after Dec 31, 2017.

Tax Reform Implications for Businesses

- Expensing and Depreciation
 - Section 179 increased to \$1 million with investment limit of \$2.5 million (NC does not conform)
 - SUVs limited to \$25,000
 - Full size crew cab ½ Ton pickups with a short box are SUVs by definition.
 - Qualified Real Property allowed
 - Roofs, HVAC, fire protection, security and alarm systems

Tax Reform Implications for Businesses

- First-year (Bonus) Depreciation
 - 100% first-year depreciation (Sept 27, 2017 – Dec 31, 2022) **Now allowed for new and used property**
 - 80% 2023
 - 60% 2024
 - 40% 2025
 - 20% 2026
 - Bonus sunsets after December 31, 2026
- North Carolina doesn't conform to Bonus**

Tax Reform Implications for Businesses

- New Farming and Machinery Depreciation
 - For property placed into service after December 31, 2017:
 - Cost recovery period is now 5 years for new machinery and equipment; used is still 7 years
 - Grain bins, fences, cotton ginning equipment, and land improvements are 7 year assets.
 - 200% declining balance is to be used on 3-, 5-, 7- and 10-year property
 - 150% declining balance on 15 and 20 year property

Tax Reform Implications for Businesses

- Limits on Deduction of Business Interest
 - Beginning after December 31, 2017, every business, regardless of form, is generally subject to a disallowance of a deduction of net interest expense in excess of 30% of the business's adjusted taxable income.
 - This is determined at the tax filer level.
 - However, for pass-through entities, the determination is made at the entity level.

Tax Reform Implications for Businesses

- Limits on Deduction of Business Interest
 - An exemption from these rules applies for taxpayers with average gross receipts for a three-tax year period ending with the prior taxable year that do not exceed \$25 million.
 - Farming businesses can elect out if they use ADS to depreciate any property used in the farming business with a recovery period of ten years or more.
 - Single purpose structures (poultry / hog houses)

Tax Reform Implications for Businesses

- Modification of Net Operating Loss Deduction
 - Generally the carry-back provisions are repealed and replaced carry forward with deduction limited to 80% of taxable income.
 - For Farmers, the 5-year carry back is modified to 2-year carry-back and then any remaining NOL can be carried forward indefinitely.
 - For losses created in tax years beginning after December 31, 2017, the NOL deduction is limited to 80% of taxable income. Carryovers are subject to this limitation too.

Tax Reform Implications for Businesses

- Domestic Production Activities Deduction (DPAD) is repealed
- DPAD replaced with Section 199A 20% deduction discussed earlier.

Tax Reform Implications for Businesses

- Like-Kind Exchanges are now LIMITED
 - Generally, for tax years beginning after December 31, 2017, like-kind exchanges are going to be allowed for real property that is not held primarily for sale (inventory)
 - Therefore, in the future, trades of equipment and machinery will be a two-step transaction:
 - Sale of traded in item at trade allowance (FMV)
 - Purchase of new item (higher basis) can use Section 179 expense or Bonus depreciation to offset tax consequence of sale.

Tax Reform Implications for Businesses

- Research and Experimentation expenses
 - Beginning for tax years after December 31, 2021, “specified R&E expenses” must be capitalized and amortized ratably over 5-year period beginning with the midpoint of the tax year in which these expense occur.

Tax Reform Implications for Businesses

- Employer's Deduction for Fringe Benefit Expenses Limited
 - Entertainment expenses are disallowed
 - The current 50% business meals deduction limit now includes “in-house cafeteria” or otherwise on the premises of the employer.
 - Not clear how this will impact farmers at this time.
 - The exclusion of income for employees for this and other such benefits is retained.

Where to from here?

- I understand that a “Technical Corrections Bill” is already in the works to address issues that emerged from the passage of the “Tax Cuts and Jobs Act”.
- The Treasury Department must issue rules and regulations pertinent to the new tax law, which are forthcoming.
- IRS will be gearing up...but they, too, are adjusting to a “new reality” as of December 22, 2017.

Questions?

- Thank you for your attention!!

Guido van der Hoeven, EA

Extension Specialist / Senior Lecturer

Email: gvanderh@ncsu.edu

Phone: 919.515.9071

Fax: 919.515.6268