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Tax reform business changes

Purpose: Use this resource to learn about key tax law changes that may impact your business clients. This resource highlights common tax topics; it is not all-inclusive. Consult the Tax Cuts and Jobs Act (TCJA) and the applicable code sections and regulations for additional guidance.

Topic	Prior law	New law	Practice tips
General			
Tax rates	• Corporate tax rates under the prior law were 15%, 25%, 34%, and 35%. The maximum tax rate of 35% applied to corporations with taxable income over $10 million. There was an additional 5% tax assessed for taxable income over $100,000 that was capped at $11,750. A 3% additional tax was assessed on taxable income over $15 million that was capped at $100,000. • Personal service corporations (PSCs) were taxed at a flat 35%.	• The new corporate tax rate is 21% effective for tax years starting Jan. 1, 2018. • There is no separate rate for PSCs. • Fiscal-year C corporations compute their tax liability for their year ending in 2018 using the blended rate approach of Sec. 15.	• With the tax rate changes, consider the appropriateness of a client's entity choice. Determine if making or terminating an S corporation election is appropriate. Many factors must be considered, including application of the new Sec. 199A qualified business income deduction, as well as state taxes.
Net operating losses (NOLs)	• Net operating losses could be carried back two years or carried forward 20 years. Special rules apply for farm NOLs.	• The carryback of NOLs is repealed effective for tax years ending after Dec. 31, 2017. • NOLs generated for years beginning after 2017 cannot reduce taxable income by more than 80%. NOLs carryforward indefinitely. Special rules apply for farm NOLs.	• Consider the 80% limitation when calculating estimated tax payments. Be sure to inform clients that they may still owe taxes despite a large NOL carryforward.
Corporate alternative minimum tax (AMT)	• A corporation was subject to AMT if its tentative minimum tax was higher than its regular federal tax.	• The corporate AMT is repealed effective for tax years beginning after Dec. 31, 2017. • New rules allow for accelerated use of any minimum tax credit (MTC) carryover.	• Consider MTCs when calculating estimated tax payments.
Partnership technical terminations	• A partnership was deemed terminated for tax purposes if there was a sale or exchange of 50% or more of the capital and profits interest in a 12-month period.	• The new tax laws repeal the Sec. 708(b)(1)(B) rule regarding technical terminations of partnerships effective Dec. 31, 2017.	

Topic	Prior law	New law	Practice tips
General *(cont.)*			
Expansion of eligibility for more favorable accounting methods	• Generally, an exception for the requirement to utilize the accrual basis of accounting existed for corporations and partnerships with C corporation partners whose average annual gross receipts were $5 million or less. • Taxpayers with inventories were exempted from accounting for those inventories for tax purposes if they had $1 million or less of average annual gross receipts (or $10 million for taxpayers in certain taxpayers). • The uniform capitalization rules were required to be applied to a taxpayer unless its average annual gross receipts were $10 million or less. The rules were required to be applied to most manufacturers, however, regardless of gross receipts.	• New provisions are effective for tax years beginning after Dec. 31, 2017. • Taxpayers subject to Sec. 448 (other than tax shelters) with three-year average annual gross receipts of $25 million or less are eligible for the cash basis of accounting. • The prior year exception defining small businesses is removed. Thus, if a business with gross receipts above the $25 million threshold drops below this threshold, it may change to the favored methods. • Taxpayers who meet the $25 million gross receipts test are not required to account for inventories under Sec. 471. Taxpayers can use a method of accounting that treats inventory items as non-incidental materials and supplies or utilize the inventory method in their "applicable financial statement" (AFS), or if they have no AFS, use the accounting procedure per books. • Small taxpayers (as defined under Sec. 448 with average annual gross receipts in the prior three-year period of $25 million or less) are excluded from all parts of Sec. 263A. • The dollar threshold for long-term contract income recognition (Sec. 460(e)) for certain construction contracts is increased to $25 million.	• Reassess client situations where the expansion of exceptions to the accrual method, inventory accounting, and uniform capitalization (Sec. 263A) may be impacted due to the increased exception threshold. • Note that entities not subject to the mandatory accrual method of Sec. 448 may still be able to use the cash method (no change). • Watch for IRS guidance on how eligible businesses change their methods of accounting.
Rules governing taxable year of inclusion	• Income generally is includible in gross income of an accrual-method taxpayer when the "all events" test is met.	• New Sec. 451(b) added the fact that the "all events" test is treated as being met no later than when the item is considered revenue for financial statement purposes.	
Conversion from S corporation to C corporation	• The Sec. 481(a) adjustment due to a terminated S corporation election had to be ratably included in income over a four-year period starting with the year the election was terminated.	• The new law allows for a Sec. 481(a) adjustment for an eligible terminated S corporation that is attributed to the revocation of the S corporation election; it will be accounted for ratably over a six-year period (beginning with the year the termination of the election is effective). • The new provision defines an eligible terminated S corporation to be any C corporation that was an S corporation at the date of enactment of the new law and it had terminated its S corporation election within two years of the law's enactment date. In addition, the owners at the time of the S corporation revocation must be the same as of the date of this law's enactment. • This provision was effective upon the enactment of the tax reform law.	• If you have S corporation clients, considering terminating their S election, determine the appropriateness of this provision to their circumstances. • Inform clients of the ownership restrictions and timing requirements to maintain their eligibility for this provision.

Topic	Prior law	New law	Practice tips
Deductions and expenses			
Domestic production activity deduction (DPAD)	• DPAD provided a 9% deduction of the qualified production activity income against taxable income.	• The new tax act repeals the DPAD effective for tax years beginning after Dec. 31, 2017.	• Communicate with clients who have benefited from this deduction; help them plan ahead.
Deductibility of interest expense	• Interest paid or accrued was deductible in determining taxable income.	• The deduction for business interest is limited to the sum of the following: business interest income, 30% of the adjusted taxable income (as defined in the new law), and the floor plan financing interest. • Any business interest not allowed due to exceeding this amount may be carried forward indefinitely. • Adjusted taxable income is determined for tax years beginning after Dec. 31, 2017 and before Jan. 1, 2022 without regard to depreciation, amortization, or depletion. • Limitations do not apply to taxpayers whose annual average gross receipts are $25 million or less.	• Clients may have an unrealistic understanding about this provision based on limited media exposure. Consider providing them an analysis of how the provision would impact them based on 2017 financial information to reduce possible anxiety. • The exception for small businesses does not include a tax shelter (Sec. 448(d)(3)).
Entertainment and transportation expenses	• Entertainment directly related to a trade or business was 50% deductible in the computation of taxable income.	• The tax act modifies the provision to disallow any deduction for: o Activities generally considered to be entertainment, leisure, amusement, or recreation o Membership dues with respect to any club organized for business, pleasure, recreation, or social purposes o Facilities used in connection with the previous two items • The act also repeals the deductibility of qualified transportation fringe benefits (such as transit passes). • Provisions are effective for amounts paid or incurred after Dec. 31, 2017. • See employee-related matters below for further discussion.	• Have client discussions about their marketing, meals and entertainment, and advertising expenses to have a more holistic understanding of clients' approach to interacting with customers. • Consider the opportunity to provide accounting services to ensure proper accounting. • Watch for IRS guidance in this area.
Limitation on executive compensation deduction	• There was a $1 million limit for compensation paid to the CEO and the top four executives of a publicly traded corporation; limitation was on base salary and did not include performance-based or deferred compensation.	• The limitation was expanded to include publicly traded corporations that are no longer required to file a proxy statement and foreign corporations traded through American Depository Receipts. The exclusion for commissions and performance-based compensation is eliminated and the limit applies to payments to former employees, beneficiaries of deceased employees, and to an ex-spouse.	
Local lobbying expenses	• Lobbying expenses are generally nondeductible, but under prior law, an exception was permitted for local legislation under certain circumstances.	• The new law repeals the exceptions for lobbying local governing bodies, including Indian tribal governments. This provision is effective on the enactment date of the new tax act (Dec. 22, 2017).	

Topic	Prior law	New law	Practice tips
Assets and depreciation			
Bonus depreciation	• Taxpayers could claim an additional first-year depreciation deduction for qualified property acquired and placed in service prior to Jan. 1, 2020. The amount of the additional deduction in 2017 was 50%, then 40% in 2018, 30% in 2019 and phased out completely in 2020. This bonus depreciation was allowable for AMT purposes as well. Taxpayers could elect out of bonus depreciation annually if their circumstances warranted it. • Bonus depreciation could be claimed for luxury autos in the amount of $8,000 for 2017, with a $1,600 reduction every year starting in 2018.	• Taxpayers are allowed to claim a 100% first-year depreciation deduction on qualified property that is acquired and placed in service after Sept. 27, 2017. Starting in 2023, there will be a phase out of 20% each year until 2027 when the first year additional depreciation is 0%. • The use of the qualified property does not have to originate with the taxpayer, which allows new and used property to qualify for bonus depreciation.	• With the provisions for bonus depreciation outlined through 2026, take this opportunity to have regular conversations with clients about their asset acquisition behavior and how that plays into their tax planning. • In evaluating whether to acquire a business via a stock or asset purchase, consider that qualified used assets are now eligible for bonus deprecation.
Expansion of Sec. 179 expensing	• Prior law allowed for $500,000 of Sec. 179 expensing starting in 2015. The amount was indexed for inflation starting in tax years beginning after Dec. 31, 2015. • The $500,000 deduction would be reduced by the amount that property acquisitions exceeded $2 million. This threshold was also indexed for inflation.	• The tax law increased the maximum Sec. 179 deduction to $1 million with the phase-out threshold for acquired property being $2.5 million. These amounts are indexed for inflation beginning after 2018. • The provision expanded the definition of eligible Sec. 179 property to include specific tangible personal property utilized in a trade or business related to furnishing lodging. • The definition of qualified real property that is eligible for Sec. 179 expensing now includes improvements to nonresidential real property such as roofs, heating, ventilation, air conditioning, fire protection, and alarm and security systems placed in service after Dec. 31, 2017.	• In conjunction with the increased bonus depreciation eligibility, consider the appropriate use of bonus depreciation versus Sec. 179 expensing in individual tax years, as well as the potential for Sec. 179 and depreciation recapture.
Passenger auto depreciation limits	• Passenger cars treated as listed property under Sec. 280F had a limit for the annual depreciation deduction. These limits were $3,160 for year one, $5,100 for year two, $3,050 for year three, and $1,875 for all subsequent years. These depreciation limits did not include any appropriate bonus depreciation.	• The new law increases the limitation on depreciation for listed property under Sec. 280F to $10,000 for the first year, $16,000 for the second year, $9,600 for the third year, and $5,760 for subsequent years. These limitations have been indexed for inflation. This provision is in effect for tax years beginning after Dec. 31, 2017.	
Like-kind exchanges (LKEs) of real property	• LKEs allow for non-recognition of gain in exchanges of property of a like-kind within established periods of time. These exchanges could include depreciable tangible property, intangible/non-depreciable personal property, or real property.	• The new law restricts the non-recognition of gain in a LKE to exchanges of real property effective for exchanges completed after Dec. 31, 2017. An exemption is allowed for exchanges where the property disposed of by the taxpayer is disposed on or before Dec. 31, 2017 or the property received in the exchange is received on or before Dec. 31, 2017.	• Make sure clients who exchange personal property understand that they will have a recognized gain on the transaction. • For real property exchanges, consider how personal property included in buildings affects the tax treatment.

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Assets and depreciation *(cont.)*			
Qualified improvement property	• Prior law had special provisions related to qualified leasehold improvements, qualified restaurant property, and qualified retail improvement property that qualified the taxpayer to utilize a 15-year recovery period. • There were limitations on whether bonus depreciation would apply, which was dependent on whether the property also met the definition of qualified leasehold improvement property.	• A technical correction is required in order for qualified improvement property to be treated as intended, i.e., 15-year recovery property. The act eliminates the specific definitions of qualified leasehold improvements, qualified restaurant improvements, and qualified retail improvements. This new provision applies for property acquired and placed in service after Dec. 31, 2017. • The new provision also allows taxpayers to utilize Sec. 179 on qualified improvement property without having to take into account whether the property is subject to a lease, whether it was placed in service more than three years after the original placed in service date of the building which is improved, or whether the improvement was for a restaurant building. • Any restaurant building property that was placed in service after Dec. 31, 2017 that does not meet the definition of qualified improvement property will not qualify for Sec. 179.	• If you have clients who were previously benefiting from the restaurant and retail improvement provisions, determine if their activities would qualify under the new qualified improvement property definitions. Consider having a conversation about the client's expansion and remodel plans (if any). • Determine the appropriate use of bonus depreciation and Sec. 179 in your tax planning.
Credits			
Credit for clinical drug testing	• Prior law allowed for a 50% credit for expenses incurred for certain drugs that would treat rare diseases; drugs referred to as "orphan drugs."	• The new law decreases the credit to 25%.	
Rehabilitation of historic property credit	• Prior law allowed for a 20% credit for expenses to rehabilitate a certified historical structure; 10% credit for rehabilitating a qualified rehabilitated building.	• The 10% credit has been repealed in the new law effective Jan. 1, 2018.	
Credit for paid family and medical leave	• No provision in prior law.	• Eligible employers can claim a credit of 12.5% of wages paid to eligible employees presuming the rate of pay for the eligible employee is at least 50% of their standard wages. The credit is increased by 0.25% for every 1% increase in the rate of pay, up to 100% (which would result in a 25% credit). • Note that the family and medical leave is defined by Sec. 102(a)(1)(a)-(e) of the Family and Medical Leave Act of 1993. Employer-provided leave that is treated as vacation leave, personal leave, or other sick leave would not qualify as family or medical leave for purposes of the credit. • The provision is in effect for Jan. 1, 2018 to Dec. 31, 2019. • The credit is not available to the extent mandated under state or local law.	• Understand your clients' approach to benefits and whether they would qualify for eligibility of the credit. • Take advantage of a planning opportunity to calculate the cost of providing eligible benefits and the offsetting available credit.

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Employee-related matters			
Employer-provided food and beverages from onsite eating facility	• Employers could provide a de minimis fringe benefit to employees by offering food and beverage through an onsite eating facility for the convenience of the employer. These fringes were not includible in the employee's gross income and were deductible.	• For periods starting after Dec. 31, 2017 and before Jan. 1, 2026, the 50% limitation on meals is expanded to include food and beverage facilities onsite for the benefit of the employer. • After Dec. 31, 2025, the cost of providing food and beverages to employees by way of an onsite eating facility are nondeductible.	
Exclusion for reimbursement of qualified moving expenses	• Taxpayers who received reimbursement for qualifying moving expenses by their employer could exclude these reimbursements from gross income.	• The new law suspends the exclusion from gross income for periods starting Jan. 1, 2018 through Dec. 31, 2025. This suspension does not apply to members of the Armed Forces.	• Employees are still likely to prefer reimbursement because the taxes they will owe on that income are less than what it would cost them to pay for their own moving expenses. • Help your clients brainstorm new opportunities to attract high-quality employees.
Qualified bicycle commuting reimbursement	• A reimbursement of $20/month could be excluded from an employee's gross income for qualifying bicycle commuting.	• This provision has been repealed effective Jan. 1, 2018 through Dec. 31, 2025.	• Note that employers may still deduct the benefit, but the reimbursement will be taxable to the employee.
Employee achievement awards	• Employee achievement awards of tangible personal property that are under a specific dollar threshold could be deductible by the employer and not included in the income of the employee.	• The new law redefines tangible personal property and excludes cash, gift cards/certificates, vacations and related expenses, tickets to entertainment events, stocks/bonds/securities, and other similar items. • The intent is to narrow the scope of the definition of eligible achievement awards.	• Discuss the changes with clients who offer these types of benefits to ensure they understand the qualifying types of awards they can still give to employees (that are excluded from the employee's income).
Stock options	• Employees generally recognized income tax in the year an employer transferred stock to the employee and the right to the stock was transferable or not subject to substantial risk of forfeiture.	• A new election is available for a qualified employee to defer the inclusion in income for qualified stock in certain situations.	• Discuss the new election possibility with clients to determine eligibility and documentation necessary for employees/employers.
Settlements related to sexual harassment and sexual abuse	• A deduction was allowed for ordinary and necessary business expenses, which could include legal settlements.	• The new law disallows a deduction for any legal settlement and the legal fees related to a sexual harassment or abuse case if those payments are subject to a nondisclosure agreement.	• Consider a firm policy to request detail on legal expenses to document what type of work is being dealt with by a client. Make it a point to understand the legal environment of clients.