

PARAGON LAW

Tax Cuts and Jobs Act Summary

MAY 2018

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Summary of Tax Reform

TAX CUTS AND JOBS ACT SUMMARY

1. INCOME TAX RATES

- a. Individual income tax rate structure replaced with 10%, 12%, 22%, 24%, 32%, 35%, and 37% tax brackets
- b. Reduction of corporate tax rate to a flat 21%
- c. Reduction in corporate dividends received deduction
- d. Estates and trusts income tax rate structure replaced with 10%, 24%, 35%, and 37% tax brackets
- e. Kiddie tax modified to effectively apply estates' and trusts' ordinary and capital gains rates to child's net unearned income

2. INFLATION ADJUSTMENTS

- a. Inflation adjustment of income tax brackets to be made based on chained CPI-U (C-CPI-U), instead of the CPI-U
- b. Chained CPI-U (C-CPI-U) replaces CPI-U in inflation adjustments of various tax parameters under the Code

3. ALTERNATIVE MINIMUM TAX

- a. Alternative minimum tax exemption amounts for individuals increased
- b. AMT adjustment for standard deduction is made retroactively inapplicable in 2016 and 2017 to net disaster losses from 2016 disaster areas
- c. Alternative minimum tax on corporations is repealed
- d. Corporate minimum tax credit (MTC) may offset regular tax liability for any tax year, and is refundable for 2018–2021

4. ACA INDIVIDUAL MANDATE

- a. Shared responsibility payment (penalty) eliminated after 2018



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5. INDIVIDUALS: DEDUCTIONS AND PERSONAL CREDITS

- a. Standard deduction is almost doubled, inflation adjustment is modified
- b. Deduction for personal exemptions for taxpayer, spouse, and dependents is suspended; return-filing and withholding requirements are modified
- c. Miscellaneous itemized deductions are disallowed
- d. Overall limitation on itemized deductions (“Pease limitation” or “3%/80% rule”) is suspended
- e. 7.5%-of-AGI floor for medical expense deduction is retroactively extended through 2018 and applied to all taxpayers
- f. Itemized deduction is limited to \$10,000 for SALT—combined state/local property, state/local/foreign income, and (if elected) general sales taxes
- g. Mortgage interest deduction acquisition debt maximum is lowered to \$750,000, deduction for home equity interest is suspended
- h. Personal casualty losses are nondeductible unless attributable to a federally declared disaster
- i. Gambling loss limitation is broadened: deduction for any expense incurred in gambling—not just gambling losses—is limited to gambling winnings
- j. Alimony won't be deductible by the payor or includible by the recipient for post-2018 divorce or separation instruments
- k. \$3,000 deduction for living expenses of members of Congress is eliminated
- l. Limit on an individual's contributions of cash to charitable organizations is increased from 50% to 60% of donor's contribution base
- m. Charitable deduction is denied for contributions to a college or university in exchange for athletic event seating rights
- n. Moving expense deduction eliminated, except for certain armed forces members
- o. Donee-reporting exception to substantiation requirement for charitable contributions is retroactively repealed
- p. Child tax credit is increased to \$2,000 and expanded and a partial credit is allowed for certain non-child dependents
- q. Refundable portion of the child tax credit is increased to \$1,400 for tax years beginning after 2017
- r. Qualifying child's social security number is required to claim child tax credit

6. INDIVIDUALS: INCOME AND EXCLUSIONS

- a. Exceptions to life insurance transfer-for-value rule don't apply to life settlement transactions
- b. Exclusion for qualified moving expense reimbursements suspended, except for armed forces
- c. Exclusion for qualified bicycle commuting reimbursement suspended
- d. Exclusion for discharge of certain student loans is broadened to include discharges on account of death or disability
- e. Special “combat zone” benefits extended retroactively to members of the armed forces performing services in the Sinai Peninsula of Egypt

7. QUALIFIED BUSINESS INCOME

- a. 20% deduction for qualified business income
- b. Application of qualified business income deduction to passthrough income (e.g., S-Corporations, partnerships, and sole proprietors)
- c. Qualified business income from Puerto Rico sources may qualify for 20% deduction

8. S CORPORATIONS

- a. Treatment of revocations of S corporation elections modified
- b. Expansion of qualifying beneficiaries of Electing Small Business Trusts (ESBTs)
- c. Charitable deductions of Electing Small Business Trusts (ESBTs) modified

9. PARTNERSHIPS

- a. Repeal of partnership technical termination rule
- b. Mandatory basis adjustment upon transfers of partnership interests amended
- c. Basis reduction for partnership charitable contributions amended

10. BUSINESS DEDUCTIONS AND CREDITS

- a. NOL deduction is limited to 80% of taxable income
- b. NOLs can't be carried back, but can be carried forward indefinitely
- c. Deduction for net business interest is limited to 30% of adjusted taxable income, with indefinite carryover
- d. Deduction for net business interest is limited to 30% of adjusted taxable income, with indefinite carryover
- e. Domestic production activity deduction (DPAD) is repealed
- f. Business deduction is denied for entertainment expenses
- g. Expenses for employer-operated eating facilities are only 50% deductible through 2025, then become nondeductible
- h. Employers can't deduct cost of providing qualified transportation fringes and other transportation benefits
- i. Denial of deduction for fines, penalties, etc., is broadened
- j. Information reporting requirements are added for government and other agencies that receive fines, penalties, etc., of \$600 or more for law violations
- k. Business expense deduction is barred for settlement of sexual abuse or harassment suit that's subject to nondisclosure agreement
- l. Business expense deduction for lobbying local governments is repealed
- m. Deduction of FDIC premiums is phased out for banks with assets over \$10 billion, eliminated at \$50 billion
- n. Employers are allowed a credit for paid family and medical leave
- o. Credit for qualified rehabilitation expenditures is limited to certified historic structures and has to be taken ratably over 5 years
- p. Orphan drug credit is reduced to 25% of qualified clinical testing expenses

- q. Reduced orphan drug credit election is available to avoid having to reduce any deduction or charge to capital account for qualified clinical testing expenses
- r. Limitation on aggregate business credits is conformed to the repeal of the corporate AMT

11. SECTION 179 EXPENSING

- a. Pre-adjustment Code Sec. 179 limits raised to \$1 million (annual limit on expensing) and \$2.5 million (annual phase-down threshold based on investment)
- b. More building improvements are made eligible to be section 179 property
- c. Otherwise-qualifying residential property no longer excluded from section 179 property
- d. \$25,000 per-vehicle limit on Code Sec. 179 expensing of SUVs is made adjustable for inflation

12. BONUS DEPRECIATION

- a. Overview—Bonus depreciation is increased to 100% (“full expensing”) and is extended and modified
- b. Bonus depreciation and other benefits for qualified property are extended
- c. Bonus depreciation increased to 100% (full expensing) with phase down generally deferred from 2018 to 2023
- d. Elective form of bonus depreciation for specified plants is extended and increased to 100% (full expensing) with phase down deferred from 2018 to 2023
- e. Used property is allowed 100% bonus depreciation (full expensing)
- f. Qualified film, television and live theatrical productions added to “qualified property” eligible for 100% bonus depreciation (full expensing)
- g. Property used in certain businesses exempt from business interest limitations is excluded from 100% bonus depreciation (full expensing)
- h. \$8,000 increase for “qualified property” in the first-year depreciation cap for passenger autos is extended
- i. Placed-in-service deadline for disregard of some bonus depreciation-eligible property under the percentage of completion method is extended
- j. Corporate election trading bonus and accelerated depreciation for otherwise-deferred AMT credits is ended (conforming to repeal of corporate AMT)

13. DEPRECIATION

- a. Eligibility of building improvements for a 15-year recovery period is expanded
- b. ADS recovery period for residential rental property is shortened to 30 years
- c. ADS depreciation for buildings (and improvements) if election is made to exempt a real property business from the business interest deduction limit
- d. 200% declining balance method of MACRS depreciation is made available for many types of MACRS farming property
- e. ADS depreciation required for 10-year-or-more MACRS property if election made to exempt farming from the business interest deduction limitation

- f. Annual caps on depreciation of passenger automobiles are raised
- g. Treatment of computer equipment as listed property is ended
- h. Normalization requirements for public utilities

14. TAX ACCOUNTING

- a. Gross receipts limit for cash-method use by C corporations (and certain partnerships) raised to \$25 million and related rules changed
- b. Gross receipts limit for cash-method use by farming C corporations (and certain partnerships) is made uniform at \$25 million and related rules are changed
- c. Alternatives to inventory accounting are made available to most small businesses meeting a \$25 million gross receipts test
- d. Small business exception to UNICAP rules is expanded to apply to producers and resellers meeting the \$25 million gross receipts test
- e. Gross receipts limit to qualify for small construction contract exception to percentage of completion method is raised to \$25 million
- f. Income inclusion for tax purposes can't be later than when included for certain financial reporting purposes
- g. Accrual basis taxpayers may defer inclusion of advance payments in income to the end of year after year of receipt if so deferred for financial reporting
- h. Code Sec. 174 research and experimental expenditures paid or incurred in tax years starting after 2021 are to be amortized over 5 years
- i. Excess business loss disallowance rule replaces limitation on excess farm loss for non-corporate taxpayers for tax years beginning after Dec. 31, 2017
- j. Production period for beer, wine, distilled spirits won't include their aging period under the UNICAP interest capitalization rules for the next 2 calendar years
- k. Minority and subsequent owners can expense certain costs of replanting citrus plants lost by reason of casualty

15. CAPITAL GAINS

- a. Breakpoints for imposition of 15% and 20% capital gains/qualified dividends rates are set as statutory dollar amounts, adjusted for inflation
- b. Certain gains from partnership profits interests held in connection with performance of investment services are short-term capital gains if held for 3 years or less
- c. Like-kind exchanges are limited to exchanges of real estate
- d. Patents, inventions, certain models or designs, and secret formulas or processes are excluded from the definition of a capital asset
- e. Cost of insurance adjustment to the basis of life insurance or annuity contracts is retroactively eliminated
- f. Tax reporting requirements added for policy sales and death benefits paid under life insurance contracts
- g. Tax-free rollover of publicly traded securities gain into "specialized small business investment companies" is repealed

16. ABLE PROGRAMS AND 529 PLANS

- a. ABLE account contribution limit is increased for contributions by account's designated beneficiary
- b. Saver's credit is allowed for ABLE account contributions by designated beneficiary
- c. Tax-free 60-day rollovers from 529 plan accounts to ABLE accounts are permitted
- d. \$10,000 per year of 529 plan account funds may be used for elementary or secondary school tuition

17. BONDS AND DEVELOPMENT INCENTIVES

- a. Exclusion of interest on advance refunding bonds is repealed
- b. New tax-credit and direct-pay bonds may not be issued
- c. Gains invested in a Qualified Opportunity Fund can be temporarily deferred and permanently excluded if the investment in the Fund is held for 10 years
- d. Chief executive officers of a state can designate low-income communities as Qualified Opportunity Zones

18. 2016 DISASTER AREA RELIEF

- a. 10%-of-AGI casualty loss threshold is retroactively made inapplicable in 2016 and 2017 to net disaster losses from 2016 disaster areas
- b. \$100 per-casualty floor on deduction is retroactively raised to \$500 in 2016 and 2017 for net disaster losses from 2016 disaster areas
- c. Non-itemizers are retroactively allowed to deduct net disaster losses from 2016 disaster areas in 2016 and 2017, via enhanced standard deduction
- d. Favorable tax treatment provided for qualified 2016 disaster area plan distributions
- e. Qualified 2016 disaster distributions to be included in gross income ratably over three years
- f. Penalty-free early retirement plan withdrawals may be made for 2016 disaster area victims
- g. Recontributions of qualified 2016 disaster distributions and continued deferral of tax on amounts previously distributed permitted
- h. Period of time is provided, during which qualified retirement plans and IRAs can provide 2016 disaster relief before adopting retroactive 2016 disaster relief amendments

19. MODIFIED TERRITORIAL SYSTEM

- a. Deduction allowed for dividends received by a corporate U.S. shareholder from a specified 10% owned foreign corporation under participation exemption system
- b. Dividends allowed as a Code Sec. 245A DRD are not treated as foreign source income for purposes of the FTC limitation

- c. Basis of stock in specified 10% owned foreign corporation reduced to the extent of Code Sec. 245A DRD in determining loss on disposition
- d. Amounts treated as dividends under Code Sec. 1248 and Code Sec. 964(e) are treated as dividends for purposes of the Code Sec. 245A DRD
- e. Transferred loss amount included in income upon transfer of foreign branch assets to a specified 10% owned foreign corporation
- f. Pre-2018 accumulated deferred foreign income must be included in Subpart F income upon transition to a participation exemption system
- g. Foreign E&P deficits reduce the pre-2018 accumulated deferred foreign income included in Subpart F
- h. Deduction for pre-2018 accumulated deferred foreign income; disallowance of foreign tax credit for deducted portion; recapture for expatriated entities
- i. A U.S. shareholder may elect to pay the net tax liability for pre-2018 accumulated deferred foreign income in installments
- j. S corporation shareholders may elect to defer net tax liability for accumulated deferred foreign income until a triggering event
- k. Six-year statute of limitation for assessment of net tax liability due to pre-2018 accumulated deferred foreign income
- l. Pre-2018 accumulated deferred foreign income excluded for purposes of REIT gross income tests; election provided to include that amount in REIT income over eight years
- m. Election not to take pre-2018 accumulated deferred foreign income into account for NOL purposes

20. SUBPART F INCLUSION FOR GLOBAL INTANGIBLE LOW-TAXED INCOME

- a. U.S. shareholders of CFCs must include their global intangible low-taxed income (GILTI) in gross income
- b. Domestic corporations allowed deduction for foreign-derived intangible income and global intangible low-taxed income
- c. 80% deemed paid foreign tax credit available for global intangible low-taxed income
- d. Separate foreign tax credit basket for global intangible low-taxed income (GILTI)

21. OTHER CHANGES TO SUBPART F

- a. Definition of U.S. shareholder of a controlled foreign corporation expanded to include 10% owner by value
- b. Subpart F constructive attribution rules allow downward attribution from foreign persons to related U.S. persons
- c. Requirement that corporation must be controlled for 30 days before Subpart F inclusions apply is eliminated
- d. Foreign base company oil-related income not included in foreign base company income
- e. Previously excluded Subpart F income withdrawn from a qualified shipping investment no longer included in U.S. shareholder's income

22. ANTI-BASE EROSION AND PROFIT-SHIFTING PROVISIONS

- a. Base erosion minimum tax added on payments to foreign related parties
- b. Limitations imposed on income shifting through intangible property transfers
- c. Repeal of active trade or business exception under Code Sec. 367
- d. Deduction is disallowed for certain related party amounts paid or accrued in hybrid transactions or with hybrid entities
- e. Excise tax on stock compensation of insiders in expatriated corporations increased
- f. Surrogate foreign corporation shareholders aren't eligible for reduced dividends rate

23. OTHER FOREIGN PROVISIONS

- a. Repeal of Code Sec. 902 and other adjustments to the foreign tax credit to account for participation exemption
- b. Taxpayers who sustain a pre-2018 overall domestic loss can elect to recharacterize as much as 100% of U.S. source income as foreign source income
- c. Addition of separate foreign tax credit basket for foreign branch income
- d. Treatment of gain or loss of foreign person from sale or exchange of partnership interests
- e. Source of income from sales of inventory determined solely on basis of production activities
- f. Fair market value method of interest expense allocation or apportionment repealed after 2017

24. INSURANCE

- a. Definition of “company's share” and “policyholder's share” amended for determining insurance company dividends received deduction and reserves
- b. Operations loss deduction for life insurance companies repealed
- c. Small life insurance company deduction repealed
- d. Amortization period for insurance companies' capitalized policy acquisition expenses increased to 15 years from 10 years
- e. Repeal of ten-year spread for life insurance companies' reserve changes
- f. Rules on computation of life insurance tax reserves amended
- g. Tax on distributions to stock life insurance company shareholders from a pre-1984 policyholders' surplus account is repealed; phased inclusion of remaining balance of policyholders' surplus account is...
- h. Increase from 15% to 25% of the proration rules for property and casualty insurance companies
- i. Elective deduction of discounted loss reserve amounts for insurance companies—and related special estimated tax payment rules—are repealed
- j. Active insurance business exception to passive foreign investment company rules requires minimum insurance liabilities amount

25. TAX-EXEMPT ORGANIZATIONS

- a. Excise tax imposed on tax-exempt organizations that pay excess compensation
- b. New excise tax imposed on investment income of private colleges and universities
- c. Tax-exempt organizations' unrelated business taxable income calculated separately for each trade or business
- d. Tax-exempt organizations' unrelated business taxable income increased by disallowed fringe benefit expenses

26. COMPENSATION

- a. Performance-based compensation and commissions are made subject to \$1 million deduction limit
- b. Definition of “publicly held corporation” subject to \$1 million compensation deduction limit is expanded
- c. Definition of “covered employee” who's subject to \$1 million compensation deduction limit is expanded
- d. Employees can elect to defer income from option or RSU stock for up to five years after vesting
- e. Cash, gift cards, and other nontangible personal property don't qualify as employee achievement awards
- f. Form W-2 must include information about deferrals and inclusions under Code Sec. 83(i)
- g. Withholding is required at highest individual rate when stock subject to Code Sec. 83(i) election is included in income
- h. Penalty imposed for employer's failure to notify employee that stock is eligible for Code Sec. 83(i) election

27. RETIREMENT PLANS

- a. Special rule allowing recharacterization of Roth IRA contributions and traditional IRA contributions does not apply to conversion contributions to a Roth IRA
- b. Rollover period for plan loan offset amounts is extended from 60 days, to tax return due date
- c. Accrual limit for length of service award plans is increased from \$3,000 to \$6,000

28. ESTATE AND GIFT TAXES

- a. Estate tax basic exclusion amount increased from \$5 million to \$10 million

29. EXCISE TAXES

- a. Payments for aircraft management services are exempted from excise taxes on taxable air transportation

30. PROCEDURE AND ADMINISTRATION

- a. Head of household filing status added to paid preparer due diligence requirements
- b. Extension of time limit for contesting IRS levy and for third party suits challenging levies

31. MISCELLANEOUS

- a. Contributions by a customer or potential customer, or by a governmental entity or civic group in a capacity other than as a shareholder, are not nontaxable contributions to capital
- b. Assignments not included in income, and contribution deductions allowed, for Alaska Native Settlement Trusts