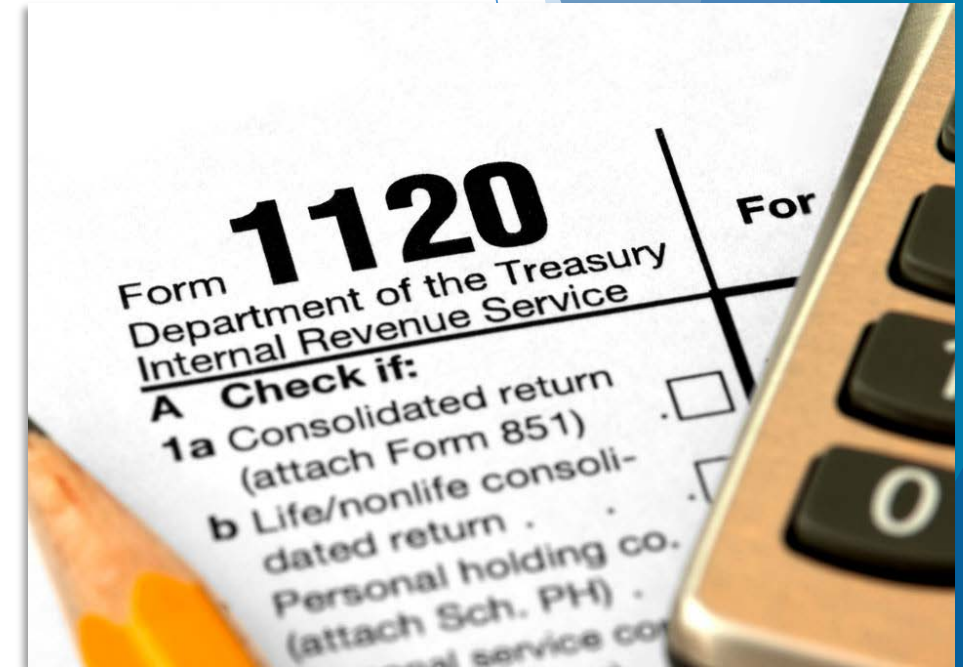


Tax Cut and Jobs Act for Businesses

What Business Owners Need to Know for 2018 & Beyond



Meet The Speaker



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Chuck Thornton, CPA specializes in tax planning, compliance and tax representation before governmental authorities. Chuck has lectured locally and nationally on topics such as tax law, management, business valuations and strategic tax planning. Both the American Institute of Certified Public Accountants and the Arizona Society of Certified Public Accountants have honored Chuck as the Speaker of the Year.

Email your questions to Chuck. If they are not answered at the end of the presentation, we will get back to you via email.

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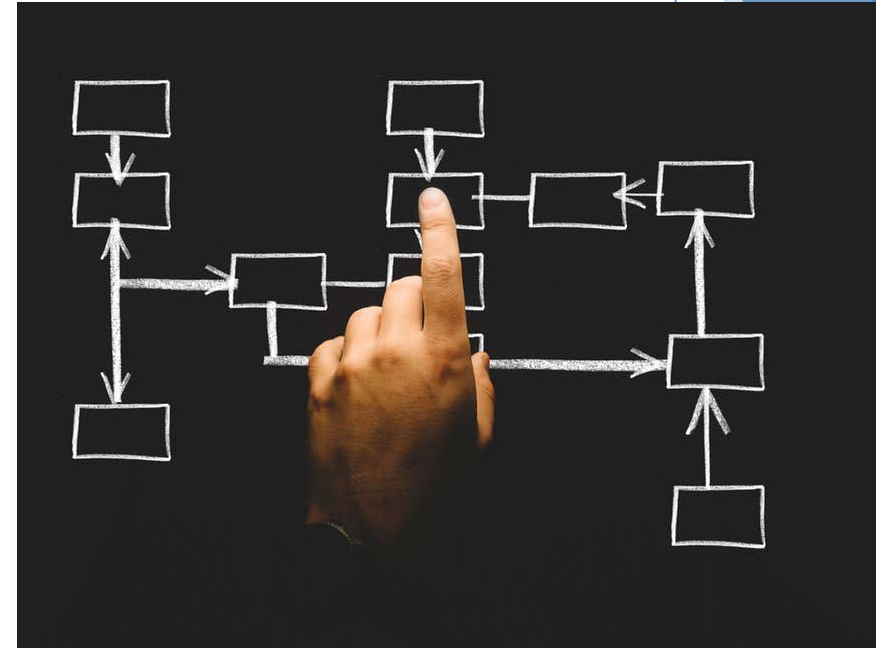


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- ▶ Chuck has made significant efforts to read, analyze and summarize important issues for individuals. This is not all inclusive. And please keep in mind that as of this seminar, the only definitive source is the internal revenue code sections and committee reports. No regulations exist as of the time of this presentation.
- ▶ Please call us if you have any questions.

Major Points We Will Discuss

- ▶ C Corporate Tax Rates
- ▶ New 20% Pass Through Deduction (Section 199A)
- ▶ Interest Paid Limitations
- ▶ Depreciation Changes
- ▶ Limitation on Losses



Corporations

- ▶ Can be a State Formed Legal Corporation
- ▶ S Election or remain a C Corporation
- ▶ Entity Elections
 - ▶ Can be S
 - ▶ Can be C



C or S Historical Positives and Negatives

▶ C Corporation

- ▶ Income at lower levels taxed at lower than individual rates—15%
However, advantage quickly evaporates
- ▶ Double Tax

▶ S Corporation

- ▶ Income pass through, sometimes initially at higher rate since individual could be higher than lower 15% discussed above
- ▶ No Double Tax
- ▶ Possible FICA Savings
- ▶ No built in Gains Tax (well maybe not)



But Now New Lower Tax Rate for C Corporations

Taxable Income	Prior Rate
Up to \$50,000	15%
\$50,001-\$75,000	25%
\$75,001-\$10,000,000	34%
\$10,000,000*	35%



But Starting in 2018

Simply 21%

Why not make all entities C- Corporations?

New C Corporate rates are basically fictitious, unless you never want to take out income

- ▶ And when you do, here is an example of what happens
- ▶ Let's use an example of a MFJ with taxable income of \$310,000

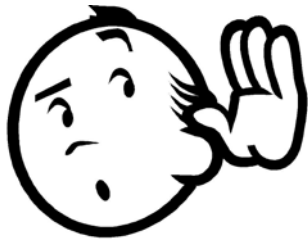
Corporate Income	\$1,000
Tax @ 21%	<u>(210)</u>
Net after tax	790
Taxed as shareholder	
Rate (new) 24%	<u>(190)</u>
Net	<u>\$600</u>

- ▶ This is an effective 40% Tax Rate!
- ▶ Had this been a Sub S the Tax Rate would be 24%!



Deduction for Qualified Business Income of Pass-thru entities

- ▶ This is the big one, and the one we will spend some time on
- ▶ Basically, (with various exceptions and limitations)
 - ▶ You get a deduction of 20% of your Qualified Business Income That is somewhat your K-1 profit.
 - ▶ So as a starter if your qualified business income is \$100,000, you get a deduction against that for 20% and hence a \$20,000 deduction
 - ▶ And if your tax bracket is 33% your tax savings is \$6,600
 - ▶ Sound interesting?



So while you're thinking of what to do with the savings, lets start with definitions.

- ▶ Qualified Business Income (QBI)(Section 199A) a new term in the code!
- ▶ QBI means income from any trade or business other than
 - ▶ A specified service trade or business, or
 - ▶ A trade or business of performing services as employee (ie W-2, so if you work for someone, Section 199A has no application to your wages.)
- ▶ What components are not part of QBI?
 - ▶ Must be associated with conduct of trade or business - watch out for Triple Net Leases
 - ▶ Does not include effectively investment income
 - ▶ Does not include Reasonable Compensation paid to tax payer (You cannot include your wages as QBI)
 - ▶ Does not include Guaranteed Payments from a Partnership.
- ▶ Big Opportunity

So while you're thinking of what to do with the savings, lets start with definitions (continued)

- ▶ What is a specified service trade or business
 - ▶ Specifically excludes engineers and architects
 - ▶ Performance of services in the field of health, law, accounting, actuarial science, performing arts, consulting, athletics, financial service broker services or any other trade or business is the reputation of skill of 1 or more employees
 - ▶ But, This will not apply under certain income ranges (discuss more on this later in another webinar)
 - ▶ Future Seminar - we will discuss Service Trade or Business - So assume for the remainder of this webinar that we are not talking about a business providing these services.



Certain Principles Apply

- ▶ QBI starts with taxable income
- ▶ Excludes investment type income
- ▶ Deduction of 20% of domestic qualified income - hence not foreign sources
- ▶ Once your total taxable income exceeds \$415,000 the deduction is further limited to the greater of
 - ▶ 50% of W-2 wages, or
 - ▶ 25% of W-2 wages plus 2.5% of unadjusted basis of property



Example

Jack files MFS. He has a Schedule C Sole Proprietorship and has taxable income from that business of \$150,000 (QBI Income). His other income is \$50,000 which is not QBI income.

- ▶ His taxable income, taking the standard deduction is \$176,000.
- ▶ Compute 20% times QBI income of \$150,000 = \$30,000 (tentative)
- ▶ Limit 20% of taxable income x \$176,000 = \$35,200
- ▶ Result \$30,000 Deduction
- ▶ BUT - Suppose his Taxable Income was \$125,000. His deduction would be limited to 20% x \$125,000 = \$25,000!

Example Taxable Income over \$415,000

- ▶ In the prior example, QBI income is \$1,000,000 (ie from proprietorship)
- ▶ No other QBI and taxable income is \$700,000
- ▶ Has W-2 wages of \$250,000—employees and even his own
- ▶ Assets with unadjusted cost of \$100,000
- ▶ Tentative deduction $\$1,000,000 \times 20\% = \$200,000$
- ▶ Limit is now NOT based on taxable income, but is based on
 - ▶ Greater of 50% wages $\$250,000 \times 50\% = \underline{\$125,000}$, or
 - ▶ 25% of W-2 wages Plus 2.5 % of unadjusted basis of assets
 $\$250,000 \times 0.25 = \$62,500$ plus $2.5\% \times 100,000 = \$2,500$ for total of $\$65,000$

Result: QBI deduction is \$125,000

Some Other Concepts

- ▶ 20% QBI from all sources is added to become “combined qualified Income”
- ▶ This can be from your share of interest in entities, as well as proprietorship
- ▶ Wage return requirement—allocable to business and for which returns filed with SSN are done before 60 days after the due date including extensions.
- ▶ 20% REIT Dividends and qualified publically trade partnership of the taxable year.

Some Other Concepts, Continued

- ▶ Qualified Property
 - ▶ Subject to Depreciation
 - ▶ Held at the close of the tax year
 - ▶ Used in the Business
 - ▶ Depreciable period has not ended before end of tax year
 - ▶ Depreciable period means a period not ending before ten years after put in place, or the last date of the recovery period - whichever is less
 - ▶ Example: 5 year property ends being qualified on 6th year
 - ▶ Example: 30 year property ends being qualified on 10th year

Qualified Income Does Not Include

- ▶ Reasonable Compensation Paid By Corporation
- ▶ Guaranteed Payments to Partners

Do you see an opportunity here?



Qualified REIT Dividend

- ▶ Means any dividend from a real estate investment trust received during year which
 - ▶ Is not a Capital Gain



Cost Recovery under Bonus Depreciation

- ▶ Prior to 1/1/2017 to 9/27/17 50%
- ▶ Acquired 9/27/2017 to 2022 100%
- ▶ Acquired 2023 80%
- ▶ Acquired 2024 60%
- ▶ Acquired 2025 40%
- ▶ Acquired 2026 20%



- ▶ Now for used or new property (which under MACRS Rules has a life less than 20 years)

179 Depreciation

- ▶ Amount of Eligible Property Increase from \$500,000 to \$1,000,000
- ▶ Phase out if more than \$2,500,000 of 179 property acquired
- ▶ Applies to new or used property



179 Definition Expansion

- ▶ Qualified tangible personal property and qualified real property
 - ▶ Improvements to non-residential real property placed in service which is
 - ▶ Roofs
 - ▶ Heating, Ventilation and Air Conditioning
 - ▶ Fire Protection and Alarm Systems
 - ▶ Security Systems

Business Interest Deduction

- ▶ Applies only to group of businesses where gross receipts exceed \$25 Million
- ▶ Disallows interest to extent it exceeds 30% of adjusted taxable income (effectively EBITDA) before interest and depreciation
- ▶ Carryforward okay
- ▶ EBITDA concept good until January 1, 2022. After that depreciation is deducted effectively creating a EBITA concept

Net Operating Loss Carryforward

- ▶ Current law NOL's carry back 2 years and forward 20 years
- ▶ Current limits income offset to 80% of future year income
- ▶ Elimination of carryback
- ▶ But NOL's can be carried indefinitely
- ▶ Reduced amount if income is over \$500,000 in carryforward year



Accounting Methods

- ▶ A process of recording transactions and keep books
- ▶ Historically at odds was a desire to use cash vs accrual
 - ▶ Cash often (but not always) better in delaying income tax (a deferral)
- ▶ New law expands universe of taxpayers that may use cash method of accounting— \$25 million gross receipts test (average over last three years)
- ▶ Now cash may, in some limits, deduct inventory (if consumed in the production process.



Percentage of Completion

- ▶ Under \$25 million gross receipts (average last three years)
- ▶ Two year test—if expect that at time contract is entered into, and contract will be completed within two years.
- ▶ This applies to contracts entered into January 1, 2018 and beyond



Contractors

- ▶ If your average receipts for the last three years is under \$25,000,000
 - ▶ You can convert to cash method first taxable year (ie if fiscal YE 12/31/18) and effectively get a deduction for your working capital, and
 - ▶ Get even bigger benefits by not having to use your percentage of completion.



Questions?

For More Information

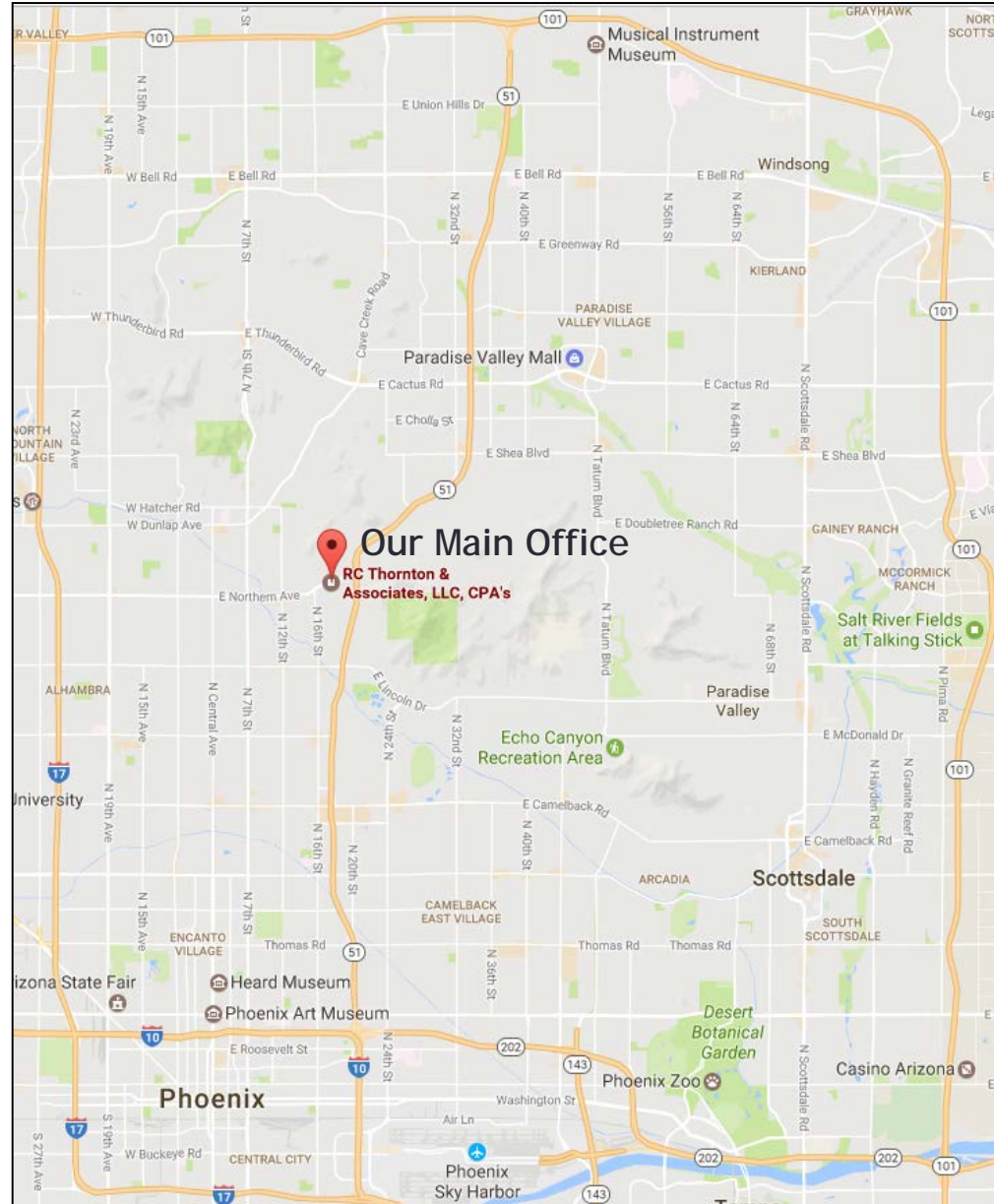
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