US tax reform: Understanding the Tax Cuts and Jobs Act
The Dbriefs Tax Reform series

Ari Berk, Principal, Deloitte Tax LLP
Harrison Cohen, Managing Director, Deloitte Tax LLP
Valerie Dickerson, Partner, Deloitte Tax LLP
Eddie Gershman, Managing Director, Deloitte Tax LLP
Craig Janes, Partner, Deloitte Tax LLP

Bob Kilinskis, Partner, Deloitte Tax LLP
Rochelle Keczynski, Partner, Deloitte Tax LLP
Jon Traub, Principal, Deloitte Tax LLP
Paul Vitola, Partner, Deloitte Tax LLP

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Agenda

Tax policy/process update
Periods, methods and credits
ASC 740
International tax provisions
Multistate considerations
Pass-through considerations
Private wealth considerations
Polling question 1

Based on what you now know about the Tax Cut and Jobs Act, which of the following best describes your thoughts on the bill?

• The lower rates and the switch to a participation exemption system are positive for me/my company

• The way the bill finances those changes is worse for me/my company than the benefits being promised

• Whatever benefits there are from the lower rates/switch to a participation exemption system don’t justify adding $1.5 trillion to the deficit

• Don’t know/Not applicable
Tax policy/process update
On Oct. 26, the House approved the Senate-passed concurrent resolution on the budget for fiscal year 2018; this was an important step because it authorized the use of budget reconciliation to reduce taxes by up to $1.5 trillion over ten years.

Congress wasted little time acting on that authority -- the House and Senate passed their respective versions of the Tax Cut and Jobs Act on Nov. 16 and Dec 2.

Two weeks ago, the House named conferees to negotiate a final agreement; the Senate followed suit two days later.

The conferees held their only public meeting on Wednesday, Dec. 13 -- both before and after intense negotiations went on behind closed doors.

On Friday, Dec. 15, conferees signed the conference report, reflecting a deal between the chambers; the text was released early that evening.
What we have here (key elements of the conference agreement)

**Business tax**

- 21% corporate rate; effective in 2018
- 20% deduction for some pass-through income
- Repeal of the corporate AMT
- Expensing for five years, phase-down after
- New limits on deductions of net business interest
- New limits on use of net operating losses
- Repeal of IRC § 199 and like-kind exchanges (other than for real property)
- Amortization of R&E costs (starting in 2022)
- Many other business changes affecting executive compensation deductions, treatment of settlement costs
What we have here (key elements of the conference agreement), cont.

**International tax**

- Shift to a participation exemption system
- One-time transition tax on previously deferred foreign E&P
- A variety of “base erosion” safeguards along with new incentives to earn foreign income on U.S.-domiciled IP
What we have here (key elements of the conference agreement), cont.

**Individual tax**

- Retain 7 tax brackets, with a top rate of 37%
- Larger standard deduction; repeal of personal exemptions
- Retain individual AMT (with higher exemption amounts)
- Double estate tax exemption amounts (but no repeal)
- New limits on deduction for state and local taxes
- Expanded child tax credit
- Limited provision affecting the tax treatment of carried interest
- Elimination of penalty for failure to purchase health insurance (the ACA’s individual mandate)
- All of these (other than ACA mandate change) sunset after the end of 2025
Where do we go from here?

House Rules Committee will meet Monday to issue a “rule” for considering the conference agreement.

House will debate the Rule for one hour and, assuming that passes, will likely have one hour of debate on the agreement itself, followed by a vote on passage – simple majority needed.

Senate provides for ten hours of debate on a reconciliation conference report, followed by a vote on passage (again, a simple majority suffices, and the Vice-President can break a tie).

No filibuster possible, but the bill must go through another “Byrd Bath” that exposes and generally results in the expungement of extraneous provisions.

Any changes resulting from the “Byrd Bath” would generally require the bill to be passed by the House a second time.

Substantive and technical changes are not possible at this point, and may be very difficult – no matter how badly needed – next year.

Could be on its way to the White House by nightfall on Wednesday; Trump is sure to sign it into law.
Periods, methods and credits
Federal tax accounting periods, methods and credits provisions in conference agreement

**Expensing**
- 100% immediate expensing for qualified property
- Phased down annually through 2026
- Longer phase down period for property with longer production period

**IRC § 199 manufacturing deduction repealed**

**Corporate AMT repealed**

**Like-kind exchanges** allowed only for real property not held primarily for sale

**Net operating losses** limited to 80% of taxable income with indefinite carryforward period (eliminates most carrybacks)

**Research and experimentation expenditures** capitalized and amortized beginning in 2022

**Changes to recovery periods for real property**

**Deferral of income**
- All-events not met later than the tax year in which the item is taken into account as revenue in an applicable financial statement, with exceptions for special methods of accounting
- Codifies the deferral method under Rev. Proc. 2004-34

**Changes to deductibility and reporting requirements for certain fines and penalties**

**Deduction for local lobbying expenses eliminated**

**IRC § 118** only applies to corporations and is left in tact, with certain exclusions

**IRC § 162(m)**
Federal credits and incentives landscape post-conference report

Most federal credits and incentives were retained without any change

Energy credits
- Investment Tax Credit for Solar
- Production Tax Credit for Wind
- Plug-in Electric Vehicle Credit
- Enhanced Oil Recovery Credit
- Marginal Well Credit

Other general business credits
- Nuclear Production Tax Credit
- Low-Income Housing Tax Credit
- New Markets Tax Credits
- Work Opportunity Tax Credit
- FICA Tip Credit
- Employer Provided Child Care Credit
- Access to Disabled Individuals Credit

Several changes to federal credits and incentives were adopted in the Conference Report

- No change in law to the Research Credit
- Modification to Base Erosion Anti-Abuse Tax (BEAT) that was part of the Senate Bill
- Creates general business credit—Employer Credit for Paid Family and Medical Leave
- Reduces the Orphan Drug Credit rate to 25% of qualified clinical testing expenses incurred in testing of certain drugs for rare diseases or conditions
- Repeals 10% Historic Rehabilitation Credit for pre-1936 buildings and reduces to 10% (from current law 20%) the tax credit for rehabilitation of certified historic structures, with modified transition rules
Rate reduction planning

- Rate reduction benefit example
- By accelerating deductions into pre-reform years / deferring revenue into post-reform years, taxpayers will likely receive a permanent tax benefit

<table>
<thead>
<tr>
<th>Potential reduction in business taxable income</th>
<th>Tax savings if deducted in 2017 at 35% rate</th>
<th>Tax savings if deducted in 2018 at 21% rate</th>
<th>Permanent tax benefit of accelerating deduction into 2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>$100,000,000</td>
<td>$35,000,000</td>
<td>$21,000,000</td>
<td>$14,000,000</td>
</tr>
<tr>
<td>$1,000,000</td>
<td>$350,000</td>
<td>$210,000</td>
<td>$140,000</td>
</tr>
</tbody>
</table>
Tax accounting planning
Category 1: Method changes for acceleration of deduction and deferral of revenue

Items that can be changed automatically:
• Deduct bonuses and vacation pay
• Inventory – Lower of cost or market/subnormal goods/reduce UNICAP costs/LIFO enhancements
• Depreciation changes
• IBNR (incurred but not reported) – self-insured medical; medical services included in workers’ compensation
• Changes to comply with Treas. Reg. § 1.263(a)-4 including prepaid expenses
• Advanced deduction of payroll taxes
• Defer advance payments – Rev. Proc. 2004-34
• Deduct software development costs
• Single item cash to accrual (does not include prepayment liabilities)
• Changes to comply with gift card guidance
• Deduct rebates and allowances under recurring item exception

Advance consent method changes:
Revenue deferral
• Unbilled revenue (see TAM 200903079)
• Changes in revenue recognition for GAAP/IFRS purposes
• Disputed receivables
• Defer advance payments – Treas. Reg. § 1.451-5
• Changes off IRC § 460

Deduction accelerations
• IBNR approach for non-medical benefit liabilities
• Identify deductible items in accruals and reserves
• The 3 ½ month rule to accelerate expense for prepaid services or property provided to the taxpayer (consider Rev. Proc. 2015-39)
• Application of recurring item exception
• Acceleration of disallowed basis under ETI and FSC (CBS Case)
Tax accounting planning
Category 2: Fact changes, including prepayment planning

Items not requiring a method change
- Inventory – expand or adopt LIFO, identify LCM write-downs
- Identify casualty and abandonment losses
- Write-off of worthless intangibles
- Accelerating payment liabilities on the sale of a business
- Disputed sales and other exclusions from income
- Depreciation – analyze placed in service dates; bonus depreciation
- Identify partially and wholly worthless bad debts
- Disposition of property through transfer to a supplies/scrap account
- Fix equity compensation deductions

Prepayment planning
- Prefund pension
- Prefund VEBA
- Make payment to Captive
- Prepay service contracts and payment liabilities
Tax accounting planning
Category 3: Other – Re-evaluate prior positions

- **IRC § 199 – planning to increase deduction**
  - Amended return opportunities for open tax years

- **Net operating losses**
  - NOL companies may consider IRC § 172(f) planning to reduce DTA for eligible 10-year carryback items (i.e., environmental liability, workers comp, product liability, land reclamation, nuclear decommissioning)
  - Amended return opportunities for open tax years
Deducting accrued bonus payments – Numerical example

Facts

- December 31, 2016 bonus accrual: $1,000,000
- Discretion exists in bonus plan
- Change number 133 filed on December 1, 2017 to change to cash basis
- Bonus plan is amended to fix the liability at December 31, 2017
- December 31, 2017 bonus accrual is $1,100,000 (paid March 1, 2018)

Effect on 2017 taxable income

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>IRC § 481(a) adjustment</td>
<td>$250,000</td>
</tr>
<tr>
<td>Deduction on cash basis for 2016 accrual</td>
<td>$(1,000,000)</td>
</tr>
<tr>
<td>Deduction for 2017 fixed bonus accrual</td>
<td>$(1,100,000)</td>
</tr>
<tr>
<td><strong>2017 deduction</strong></td>
<td><strong>$(1,850,000)</strong></td>
</tr>
</tbody>
</table>
Corporate rate change hypothetical example

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Defer revenue/advance payments</td>
<td>$ 5 million</td>
</tr>
<tr>
<td>Defer disputed income</td>
<td>$ 3 million</td>
</tr>
<tr>
<td>Specific bad debt deduction</td>
<td>$ 2 million</td>
</tr>
<tr>
<td>Accelerate prepaid insurance</td>
<td>$ 2 million</td>
</tr>
<tr>
<td>Accelerate depreciation</td>
<td>$ 5 million</td>
</tr>
<tr>
<td>Accelerate self-insured IBNR</td>
<td>$ 1 million</td>
</tr>
<tr>
<td>Accelerate rebates, returns, &amp; allowances</td>
<td>$ 3 million</td>
</tr>
<tr>
<td>Change in fact opportunities</td>
<td>$ 4 million</td>
</tr>
<tr>
<td><strong>Total taxable income deferral</strong></td>
<td><strong>$25 million</strong></td>
</tr>
</tbody>
</table>

**Benefits:**
$3.5 Million = (35% - 21% = 14% x $25 million)

- Permanent cash: $3.5 million
- Effective tax rate benefits
- Estimated tax payment benefits
- General cash flow benefits
ASC 740
Polling question 2

Of the following provisions in the tax reform legislation, which one will most significantly impact your financial statement reporting?

• Paying for a participation exemption system (i.e., minimum tax rules and/or a deemed repatriation transition tax)
• Business rate reduction
• Global intangible low-tax income (GILTI)
• Changes to the tax treatment of corporate debt
• Other business changes (i.e., limits on deductions/credits)
• All of the above
• Don’t know/Not applicable
Effect of tax law changes

**Timing [ASC 740-10-25-47]**

Income tax effects of changes in tax law or rates are not recognized until enacted

- Existing deferred tax assets and/or liabilities at enactment date – impact recognized as discrete item in period change enacted
- Current year taxes payable/refundable – tax effect is recorded after effective date and reflected in AETR no earlier than period that includes enactment date

**Intraperiod allocations**

Income tax effects of changes in tax law or rates are allocated to continuing operations (IFRS requires backward tracing)
Potential impact of select proposed changes – Upon enactment

1. **Corporate rate reduction**
   - Re-measure deferred taxes and valuation allowance, if applicable
   - Impact on ETR/AETR

2. **Deemed repatriation ("transition tax")**
   - Calculate tax payable
   - Calculation of “cash”
   - E&P and foreign tax pools
   - Remeasure any existing outside basis DTLs
   - Assess impact on valuation allowance

3. **Global intangible low-taxed income ("GILTI")**
   - Impact on deferred taxes and valuation allowance
   - Impact on ETR/AETR

4. **Base Erosion Anti-Abuse Tax ("BEAT")**
   - Impact on deferred taxes and valuation allowance
   - Impact on ETR/AETR

5. **Consider impact on valuation allowance for the following items:**
   - Business interest expense limitations
   - Lost or modified business expense deductions
   - Modifications to net operating loss deductions
Is the indefinite reinvestment assertion still relevant?

**Outside basis differences (e.g., indefinite reinvestment) still need to be considered**
Tax reform does not change U.S. GAAP requirement to consider whether deferred taxes should be recorded for outside basis differences in investments in foreign subsidiaries and corporate joint ventures that are permanent in duration.

**Foreign tax considerations**
- Consider all entities in the organization chart
- Withholding taxes – DTLs may need to be recorded for withholding taxes and state taxes if distributions are anticipated.

**US federal and state tax considerations**
While some basis differences may not represent taxable temporary differences due to 100% DRD, others might. For example,
- Capital gains – still taxable in the US
- IRC § 986(c) – Foreign currency gain or loss with respect to distributions of previously taxed income
- State taxes – DTLs may need to be recorded for state taxes if distributions are anticipated
- GILTI – Consider whether the provisions could potentially have an impact on indefinite reinvestment assertion.
Financial statement disclosure considerations

**Footnote disclosures**

**Enactment before reporting date:**
- Income statement – Disclose significant components of income tax expense attributable to continuing operations, including adjustments of deferred tax assets/liabilities for enacted changes in tax laws or rates
- Disclose nature and effect of significant matters affecting comparability of information for all periods presented, if not otherwise evident

**Enactment after reporting date but before financial statements issued:**
- Non-recognized subsequent events – Disclose impact to keep financial statements from being misleading and estimate of impact of new law to determine disclosure

**SEC disclosures**
- SEC Reg. S-K (“Risk Factors”) requires disclosures of significant risks that could impact company in future
- SEC Reg. S-K (“MD&A”) requires disclosures of trends or uncertainties reasonably expected to have a material favorable/unfavorable impact
International tax provisions
Polling question 3

How prepared is your organization for the shift to a participation exemption tax system, including computing the transition tax and complying with new “base erosion” prevention rules?

• Fully prepared
• Somewhat prepared
• Not prepared
• Don’t know/Not applicable
Participation exemption (IRC § 245A)

- 100% DRD for the “foreign-source portion” of dividends received by domestic corporations from “specified 10% owned foreign corporations”
- “Hybrid dividends” not allowed the DRD
- Hybrid dividends received by one CFC from another CFC treated as subpart F income
- Minimum 366-day holding period
- Effective for distributions made after 2017
Transition tax

**Transition tax (IRC § 965)**

- Applies to US shareholders of “specified foreign corporations” (“SFCs”)
- Tax rates: 15.5% to extent of (corporate) US shareholder’s pro rata shares of SFCs’ cash assets / 8% on remainder; proportional reduction in resulting deemed-paid taxes of corporate US shareholders
- Determine SFC’s accumulated post-1986 foreign deferred earnings as of November 2 and December 31, without diminution by dividends distributed in its last tax year beginning before 2018 (other than dividends distributed to another SFC)
  - The greater number is added to the SFC’s subpart F income for its last year beginning before 2018
Transition tax

**Transition tax (IRC § 965)**

- US shareholder has income inclusion under IRC § 951(a)
  - Inclusion reduced by shareholder’s pro rata shares of SFCs’ deficits in post-1986 E&P as of November 2
- Secretary given authority to issue regulations to address double counting and non-counting of E&P, or to prevent the avoidance of the purposes of IRC § 965
- Election to pay over 8 years
- Additional timing accommodations relating to S corporations and REITs
- Generally applies to individuals as well as corporations
- Effective for the last tax year of a foreign corporation that begins before 2018, and with respect to US shareholders, for the tax years in which or with which such tax years of foreign corporations end
Global intangible low-taxed income (GILTI)

US shareholder inclusion for GILTI (IRC § 951A) and corporate GILTI deduction (IRC § 250(a)(1)(B))

- US shareholder of CFCs includes in gross income its “global intangible low-taxed income” (“GILTI”)
- Corporate US shareholder (other than RIC or REIT or S corp) generally allowed a deduction 50% of GILTI inclusion (37.5% for taxable years beginning after 2025)
- Deduction (together with the FDII deduction) limited by taxable income
- GILTI = excess (if any) of
  - The shareholder’s “net CFC tested income” over
  - The shareholder’s “net deemed tangible income return”
Global intangible low-taxed income (GILT)

US shareholder inclusion for GILT (IRC § 951A) and corporate GILT
deduction (IRC § 250(a)(1)(B))

- Net deemed tangible income return = excess (if any) of
  - 10% of the aggregate of shareholder’s pro rata shares of the qualified business asset investment (QBAI) of CFCs, over
  - Interest expense taken into account in determining shareholder’s net CFC tested income for the taxable year (to the extent that the interest income attributable to such expense is not taken into account in determining its net CFC tested income)

- Net CFC tested income = excess (if any) of
  - Aggregate pro rata shares of CFCs’ tested incomes, over
  - Aggregate pro rata shares of CFCs’ tested losses
Global intangible low-taxed income (GILTI)

**US shareholder inclusion for GILTI (IRC § 951A) and corporate GILTI deduction (IRC § 250(a)(1)(B))**

- A CFC’s tested income (or loss) is its gross income (excluding certain amounts) less allocable deductions (including taxes)
- Exclusions:
  - ECI
  - Gross subpart F income
  - Gross income excluded from subpart F by the high tax exception
  - Dividends from related persons
  - FOGEI
- Foreign tax credits: Corporate US shareholder is deemed to pay 80% of the “inclusion percentage” × the foreign income taxes paid by each CFC that is attributable to the CFC’s tested income, if any, taken into account by the shareholder under IRC § 951A
  - “Inclusion percentage” is the ratio of the shareholder’s GILTI to the aggregate of its CFCs’ tested incomes
  - Separate basket; no carryovers
- Effective for tax years of foreign corporations beginning after 2017 and for tax years of US shareholders in which or with which such tax years of foreign corporations end
Corporate deduction for foreign-derived intangible income (FDII)

**Deduction for domestic corporations’ “foreign-derived intangible income” (“FDII”)**

- Subject to taxable income limitation, domestic corporation generally entitled to deduction for 37.5% (21.875% for tax years beginning after 2025) of foreign-derived intangible income
- Effective for tax years beginning after 2017

\[
\text{FDII} = (\text{DEI} - \text{DTI}) \times \frac{\text{FDDEI}}{\text{DEI}}
\]

Where--

**DEI** stands for “deduction eligible income”

**DTI** stands for “deemed intangible income”: the excess of DEI over 10% QBAI used to produce DEI

**FDDEI** stands for “foreign-derived deduction eligible income”
Corporate deduction for foreign-derived intangible income (FDII)

**Deduction for domestic corporations’ “foreign-derived intangible income” (“FDII”)**

- DEI—“deduction eligible income”:
  - The excess of the gross income of the corporation, determined without regard to certain amounts, over the deductions (including taxes) properly allocable to such gross income.
  - Exceptions:
    - IRC § 951(a)(1) inclusions
    - IRC § 951A inclusions
    - Financial services income
    - Dividends from CFCs
    - Domestic oil and gas extraction income
    - Foreign branch income
Corporate deduction for foreign-derived intangible income (FDII)

**Deduction for domestic corporations’ “foreign-derived intangible income” (“FDII”)**

- **FDDEI**—“foreign-derived deduction eligible income”: generally, DEI derived in connection with
  - Property “sold” by the taxpayer to any person who is not a US person and that the taxpayer establishes to the satisfaction of the Secretary is for a foreign use, or
  - Services provided by the taxpayer that the taxpayer establishes to the satisfaction of the Secretary are provided to any person, or with respect to property, not located within the United States
    - Special rules for related-party transactions; “sold” includes “licensed” and “leased”
- Only C corps (not RICs and REITs) can take deduction for FDII
- Effective for tax years beginning after 2017
Base erosion and anti-abuse tax ("BEAT")

Base erosion and anti-abuse tax ("BEAT") (IRC § 59A)

- Imposes, on corporation that is an "applicable taxpayer," a tax equal to its "base erosion minimum tax amount" ("BEMTA")
- BEMTA is the excess of:
  - Percentage (see below) of "modified taxable income" ("MTI") over
  - Regular tax liability reduced by certain credits
- Percentage: for tax years beginning—

<table>
<thead>
<tr>
<th></th>
<th>Taxpayers generally</th>
<th>Banks and securities dealers</th>
</tr>
</thead>
<tbody>
<tr>
<td>in 2018</td>
<td>5%</td>
<td>6%</td>
</tr>
<tr>
<td>after 2018 and before 2026</td>
<td>10%</td>
<td>11%</td>
</tr>
<tr>
<td>after 2025</td>
<td>12.5%</td>
<td>13.5%</td>
</tr>
</tbody>
</table>
Base erosion and anti-abuse tax ("BEAT")

Base erosion and anti-abuse tax ("BEAT") (IRC § 59A)

- Prior to 2026, the following credits do not reduce regular tax liability for BEMTA computation purposes:
  - 80% of low-income housing credit, renewable electricity production credit, energy credit
  - 100% of research credit
- MTI = taxable income without regard to
  - deductions ("base erosion tax benefits") for certain payments made to related foreign persons that give rise to deductions ("base erosion payments" (BEPs)), and
  - the “base erosion percentage” of the NOL deduction
- In the case of companies that become “inverted” after November 9, 2017, base erosion payments can also include cost of goods sold
Base erosion and anti-abuse tax ("BEAT")

Base erosion and anti-abuse tax ("BEAT") (IRC § 59A)

• To be an “applicable taxpayer,” the “base erosion percentage” must be at least 3% (2% for banks), and average annual gross receipts for the prior 3 years must be at least $0.5 billion (both computed on a group-wide basis)

• Payments for services at “cost” (with no markup) may be excluded from BEPs

• Taxpayers that mark derivatives to market (e.g., certain dealers) may be entitled to exclude “qualified derivative payments” from BEPs

• Applies to base erosion payments paid or accrued in tax years beginning after 2017
International tax provisions eliminated in conference

Amendments to the Internal Revenue Code that were passed by one or both houses of Congress but were eliminated from the bill by the conference agreement

• Proposed modifications to existing subpart F rules:
  o Proposal to make IRC § 954(c)(6) “CFC look-thru rule” permanent
  o Proposed repeal of IRC § 956 with respect to corporate US shareholders
  o Proposed inflation adjustment of de minimis exception (IRC § 954(b)(3)) for foreign base company income

• Proposed international group-based limitations on interest deductions (proposed new IRC § 163(n))

• Proposed rules for the tax-free repatriation of intangible property (proposed new IRC § 966)
Senate-only international tax provisions adopted in conference

Provisions that were added to the bill by the Senate and were included in the conference agreement

- Repeal of the “active trade or business” exception (IRC § 367(a)(3)) from the general non-recognition override provision for certain outbound transfers (IRC § 367(a)(1))
- Amend the definition of intangible property (IP) in IRC § 936(h)(3)(B) to include workforce in place, goodwill, and going concern value
- Provide explicit statutory authority for IRS to value IP on an aggregate basis (“aggregate basis valuation”), if doing so would achieve a more reliable result than an asset-by-asset approach, and to determine an arm’s length price by reference to a transaction different from the one actually completed (“realistic alternatives principle”)
- Provide separate IRC § 904 limitation “basket” for foreign branch income
- Eliminate the fair market value method for allocating interest expense under IRC § 864(e)
- Modify the stock attribution rules under subpart F, and allow “downward attribution” of stock owned by foreign persons to US persons, effective for a foreign corporation’s last tax year beginning before 2018 and each subsequent year
- Expand subpart F definition of “US shareholder” to include US person who owns 10% or more of the value of a foreign corporation
International tax provisions common to both bills and retained in conference

Provisions that were passed by both houses and included in the conference agreement

- Repeal IRC § 902 (relating to foreign taxes deemed paid by corporations upon receipt of dividends from foreign corporations)
- Eliminate the “pooling” principle from IRC § 960 (relating to foreign taxes deemed paid by corporations upon receipt of subpart F inclusions)
- Source IRC § 863(b) sales income based solely on place of production
- Repeal IRC § 955 (taxing certain CFC withdrawals of investment in shipping operations)
- Repeal foreign base company oil related income as a type of subpart F income
- Eliminate 30-day requirement for subpart F inclusion
- Restrict the insurance business exception to the PFIC rules
Polling question 4

Of the following, which does your organization view as the most critical action in response to final legislation around international tax?

• Quantifying the financial statement impact for the period ending December 31, 2016
• Efficiently funding the payment of the transition tax
• Restructuring cross-border operations
• Identifying uses of funds that will be newly available for tax-free repatriation
• None of the above
• Don’t know/Not applicable
Multistate tax considerations
## Tax reform: Multistate tax considerations

<table>
<thead>
<tr>
<th>Provision</th>
<th>“To-Do”</th>
</tr>
</thead>
</table>
| **Federal corporate rate reduction**          | • Analyze state deferred tax asset inventory  
• Evaluate impact of proposed federal accounting method changes/other decisions to accelerate deductions/defer income and update plans to enhance utilization of state deferred tax assets  
• Consider accelerating payment of known state tax liabilities:  
  o Voluntary disclosure/amnesty  
  o Resolve state tax disputes  
  o RAR reporting                                                                                                                      |
| **Immediate federal expensing**              | • Evaluate state conformity to IRC § 168(k)  
• Coordinate taxpayer planning (i.e., immediate expensing and repatriation) of foreign E&P  
• Identify state and local C&I opportunities                                                                                               |
| **Elimination/modification of federal deductions/credits** | • Evaluate state conformity to repeal of/limitations on federal incentives  
• Evaluate state-specific opportunities for similar incentives (e.g., state-specific WOTC)                                                   |
## Tax reform: Multistate tax considerations

<table>
<thead>
<tr>
<th>Provision</th>
<th>“To-Do”</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Repatriation</strong>&lt;br&gt;Rates: 15.5%/8% for cash/non-cash</td>
<td>• Model impact of increased Subpart F income recognition for state taxes; develop plan for managing state exposure  &lt;br&gt;  • Calculate inventory of pre-deemed repatriation and post-repatriation foreign E&amp;P &lt;br&gt;  • Develop plan for actual repatriation</td>
</tr>
<tr>
<td><strong>Federal tax on “Global Intangible Low-Taxed Income” (“GILTI”) and related deduction under new IRC § 250</strong></td>
<td>• Evaluate state conformity to new IRC §§ 250 and 951A &lt;br&gt;  • Evaluate state income tax treatment of GILTI/IRC § 250 deduction &lt;br&gt;  • Evaluate current state taxation of GILTI (e.g., WW, 80/20, etc.) &lt;br&gt;  • Consider structuring and other tax planning options</td>
</tr>
<tr>
<td><strong>Federal “base erosion anti-abuse tax” (“BEAT”) on taxable income in excess of deductible payments to related foreign parties</strong></td>
<td>• Potential for state legislative action to conform to new IRC § 59A unclear &lt;br&gt;  • Consider state add-back provisions &lt;br&gt;  • Consider state implications of structuring and other tax planning options</td>
</tr>
</tbody>
</table>
## Tax reform: Multistate tax considerations

<table>
<thead>
<tr>
<th>Provision</th>
<th>“To-Do”</th>
</tr>
</thead>
</table>
| 100% DRD on repatriated foreign E&P (the new participation exemption system) | • Under current law, general conformity to new IRC Section 245A may occur  
• For states that may include, consider potential applicability of differing state treatment of distributions from unitary and non-unitary foreign affiliates |
| Limitations on federal income tax deduction for interest                  | • Evaluate state conformity to proposed amendments to IRC § 163(j) imposing limits on deductions for interest expense  
• Evaluate state impact of taxpayers shifting away from debt (e.g., franchise taxes) |
| Net operating loss modifications                                           | • NOL deductions limited to 80% of taxpayer’s (pre-NOL) taxable income  
• Most carrybacks eliminated  
• Indefinite carryforward allowed  
• House proposal to adjust carryforwards for time value of money not adopted |
## Tax Reform: Multistate Considerations

<table>
<thead>
<tr>
<th>Provision</th>
<th>“To-Do”</th>
</tr>
</thead>
</table>
| **Pass-through income**<br>(New 20% deduction for qualified business income) | • Evaluate state conformity to new qualified business income (QBI) deduction and new IRC § 199A (including states already imposing entity-level income taxes on passthroughs)  
• Consider state impact of restructuring that could follow federal corporate rate reduction below pass-through income rates  
• Evaluate federal QBI definition in new IRC § 199A and taxpayer apportionment/ allocation determinations for state business/non-business income purposes |
| **State and local C&I leading to taxable contributions to capital** | • Identify taxpayer assets subject to state and local C&I  
• Calculate potential federal income tax exposure that could result if inventoried assets transferred via capital contribution  
• Evaluate state conformity to amended IRC § 118  
• Consider whether contributions to capital could be made prior to enactment of the Tax Cut and Jobs Act |
Pass-through considerations
Pass-through considerations

Income tax deduction for non-corporate taxpayers

The deduction

• For taxable years beginning after 12/31/17, income tax deduction for the “Combined QBI” of individual taxpayers:
  - 20% of QBI for each “qualified trade or business,” subject to W-2 wage and basis limitations discussed later, plus
  - 20% of any qualified REIT dividends, qualified cooperative dividends, and qualified publicly traded partnership income

Qualified business income (“QBI”)

• QBI is net income effectively connected with a qualified U.S. trade or business included in determining taxable income
• If aggregate QBI is positive, then a deductible amount is calculated separately for each trade or business and included in the taxpayer’s combined QBI amount
• If aggregate QBI is negative, then net loss is carried forward to succeeding year
• Excludes short-term and long-term capital gains and losses, dividends and dividend equivalents, certain commodity gains and losses, certain foreign currency gains and losses, certain notional principal contract income, and interest income or annuity income that is not business related
• Excludes deduction or loss that is properly allocable to any excluded income items above
• Excludes reasonable compensation paid to S corporation shareholders, IRC § 707(c) guaranteed payments for services, and non-partner capacity payments (under regulations)
Income tax deduction for non-corporate taxpayers

Qualified trade or business

- Any trade or business, other than –
  - A specified service trade or business, or
  - The trade or business of performing services as an employee
- Specified service trade or business means any trade or business:
  - Involving the performance of services in the fields of health, law, accounting, actuarial science, performing arts, consulting, athletics, financials services, or brokerage services (this list specifically excludes engineering and architecture),
  - Where the principal asset of such trade or business is the reputation or skill of 1 or more of its owners or employees, or
  - Which involves the performance of services that consist of investing and investment management, trading, or dealing in:
    - Securities (as defined in IRC § 475(c)(2)),
    - Commodities (as defined in IRC § 475(e)(2)), or
    - Partnership interests
- However, the exception for a specified service trade or business does not apply if the taxpayer has less than $315,000 (MFJ) or $157,000 (all other filers) of taxable income before deduction. The benefit of the deduction is phased out over the next $100,000 (MFJ) or $50,000 (all other filers) of taxable income before deduction
- Unclear how a trade or business is determined and whether there will be grouping rules similar to IRC § 469 or, instead, rules similar to IRC § 446
Income tax deduction for non-corporate taxpayers

W-2 wage and basis limitation

• The deductible amount for each trade or business is limited to the greater of:
  o 50% of W-2 wages with respect to the qualified trade or business, or
  o 25% of W-2 wages, plus 2.5% of the unadjusted basis immediately after acquisition of all qualified property

• W-2 wages are amounts paid with respect to employment of employees (and reported to SSA) during the calendar year ending during the taxable year and allocable to the QBI

• Qualified property is tangible property that is subject to depreciation:
  o Which is held by, and available for use in, the qualified trade or business at the close of the taxable year,
  o Which is used at any point during the taxable year in the production of qualified business income, and
  o The depreciable period for which has not ended before the close of the taxable year (depreciable period begins on the date the property was first placed in service by the taxpayer and ends either 10 years later or on the last year of the actual recovery period, whichever is later)

• The W-2 wage and basis limitation does not apply to taxpayers with less than $315,000 (MFJ) or $157,500 (all other filers) of taxable income before deduction, but the limitation is phased in over the next $100,000 (MFJ) or $50,000 (all other filers) of taxable income before deduction
Income tax deduction for non-corporate taxpayers

Other rules

• Application to partnerships and S corporations:
  o Provisions are applied at the partner or shareholder level,
  o Each partner or shareholder takes into account the partner’s or shareholder’s “allocable share” of each qualified item of income, gain, deduction, and loss,
  o Each partner or shareholder is treated as having their share of the partnership’s or S corporation’s total W-2 wages (determined in the same manner as the partner’s or shareholder’s “allocable share” of wage expenses), and
  o Each partner or shareholder is treated as having their share of the partnership’s or S corporation’s “unadjusted basis immediately after acquisition of qualified property” for the taxable year (determined in the same manner as the partner’s or shareholder’s “allocable share” of depreciation expense)

• Application to trusts and estates:
  o Unlike previous versions of the bill, the deduction is available to trusts and estates
  o Rules from the repealed IRC § 199 deduction are used to apportion W-2 wages and “unadjusted basis immediately after acquisition of qualified property”

• For individual taxpayers, the deduction does not reduce AGI, but is available to taxpayers who itemize or use the standard deduction

• The deduction does NOT apply to taxable years beginning after December 31, 2025
## Choice of entity–Rate differences

<table>
<thead>
<tr>
<th>Entity</th>
<th>Formula</th>
<th>Top marginal tax rate</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Existing law</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Passive C Corp Shareholder&lt;sup&gt;1&lt;/sup&gt;</td>
<td>Corp Rate (35%) + (65% * (QDI Rate (20%) + NII Rate (3.8%)))</td>
<td>50.47%</td>
</tr>
<tr>
<td>Active&lt;sup&gt;2&lt;/sup&gt; C Corp Shareholder</td>
<td>(90%<em>35%) + (58.5%</em>(20%+3.8%)) + (10%*(39.6%+SE Rate&lt;sup&gt;3&lt;/sup&gt;(3.8%))</td>
<td>49.76%</td>
</tr>
<tr>
<td>Passive Partner</td>
<td>Indiv. Rate (39.6%) + NII Rate (3.8%)</td>
<td>43.40%</td>
</tr>
<tr>
<td>Active&lt;sup&gt;2&lt;/sup&gt; Partner&lt;sup&gt;5&lt;/sup&gt;</td>
<td>(90%<em>39.6%) + (10%</em>(39.6%+3.8%))&lt;sup&gt;6&lt;/sup&gt;</td>
<td>39.98%</td>
</tr>
<tr>
<td><strong>Final bill</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Passive C Corp Shareholder</td>
<td>Corp Rate (21%) + (79%*(QDI Rate (20%)+NII Rate (3.8%)))</td>
<td>39.80%</td>
</tr>
<tr>
<td>Active&lt;sup&gt;2&lt;/sup&gt; C Corp Shareholder</td>
<td>(90%<em>21%) + (71.1%</em>(20%+3.8%)) + (10%*(37%+3.8%))</td>
<td>39.90%</td>
</tr>
<tr>
<td>Passive Partner (No Wages)&lt;sup&gt;4&lt;/sup&gt;</td>
<td>(100%-[199A deduction (100%*0%)]) * (37%+3.8%)</td>
<td>40.80%</td>
</tr>
<tr>
<td>Passive Partner (Enough Wages)</td>
<td>(100%-[199A deduction (100%*20%)]) * (37%+3.8%)</td>
<td>32.64%</td>
</tr>
<tr>
<td>Active&lt;sup&gt;2&lt;/sup&gt; Partner&lt;sup&gt;5&lt;/sup&gt; (No Wages)&lt;sup&gt;4&lt;/sup&gt;</td>
<td>((90%-[199A deduction (90%*0%)])<em>37%) + (10%</em>(37%+3.8%))&lt;sup&gt;6&lt;/sup&gt;</td>
<td>37.38%</td>
</tr>
<tr>
<td>Active&lt;sup&gt;2&lt;/sup&gt; Partner&lt;sup&gt;5&lt;/sup&gt; (Enough Wages)</td>
<td>((90%-[199A deduction (90%*20%)])<em>37%) + (10%</em>(37%+3.8%))&lt;sup&gt;6&lt;/sup&gt;</td>
<td>30.72%</td>
</tr>
<tr>
<td>Active&lt;sup&gt;2&lt;/sup&gt; S Corp S/H (Only S/H Wages)</td>
<td>((90%-[lesser of (10%*50%) or (20%*90%)])<em>37%) + (10%</em>(37%+ 3.8%))&lt;sup&gt;7&lt;/sup&gt;</td>
<td>37.01%</td>
</tr>
<tr>
<td>Active&lt;sup&gt;2&lt;/sup&gt; S Corp S/H (Enough Wages)</td>
<td>((90%-[199A deduction (90%*20%)])<em>37%) + (10%</em>(37%+3.8%))&lt;sup&gt;7&lt;/sup&gt;</td>
<td>30.72%</td>
</tr>
</tbody>
</table>

1. For corporate scenarios, assuming that all after tax earnings distributed
2. Assumes 10% of income is paid as compensation to shareholder or partner
3. For simplicity, the employment tax rate is assumed to be 3.8% and payroll tax deductions are ignored
4. The scenarios without any employee wages also represent the top marginal rate for specified service businesses
5. Assumes that the limited partner exception applies
6. Assumes a 100% partner
7. Assumes a 100% shareholder
Carried interest
Three-year holding period requirement

- Treats the amount of a taxpayer’s net long-term capital gain with respect to an applicable partnership interest over the taxpayer’s net long-term capital gain with respect to such interest computed by substituting “3 years” for “1 year” for paragraphs (3) and (4) of IRC § 1222 as short-term capital gain

- Likely applicable to both distributive share of LTCG and gain from the disposition of the API (with the holding period likely tested at the level of disposition)

- Regulatory authority to provide that the three-year holding period requirement does not apply to income or gain attributable to any asset not held for portfolio investment on behalf of “third party investors”

- Applicable to taxable years beginning after 12/31/17
Carried interest

Applicable partnership interest ("API")

- Any interest in a partnership which, directly or indirectly, is transferred (or is held by) the taxpayer in connection with the performance of substantial services by the taxpayer, or any other related person, in any applicable trade or business (ATB)

- An API does not include:
  - An interest held directly or indirectly by a corporation
  - A capital interest if the taxpayer shares in partnership capital commensurate with (i) the amount of capital contributed (determined at the time of the receipt of that partnership interest) or (ii) the value of that interest subject to tax under IRC § 83 upon the receipt or vesting of that interest; or
  - An interest held by a person who is employed by another entity that is conducting a trade or business (other than an ATB) and only provides services to that other entity (presumably applies to a situation where a partnership issues a profits interest to an employee of the partnership’s corporate subsidiary)
Carried interest (cont.)

**Applicable Trade or Business**

- Any activity conducted on a regular, continuous, and substantial basis which consists, in whole or in part, of
  - Raising or returning capital; and
  - either (i) investing in (or disposing of) specified assets (or identifying specific assets for such investing or disposition), or (ii) developing specified assets

**Specified Asset**

- Securities (as defined in IRC § 475(c)(2) but not excluding IRC § 1256 contracts)
- Commodities (as defined in IRC § 475(e)(2))
- Real estate held for rental or investment
- Cash or cash equivalents
- Options or derivative contracts with respect to any of the above, and
- An interest in a partnership to the extent of the partnership’s proportionate interest in any of the above
Carried interest

Other rules

• Gain recognized on the transfer of an API to a related person is recharacterized as short-term capital gain to the extent of the excess of:
  o The taxpayer’s long-term capital gain attributable to the sale or exchange of any asset held for not more than three years as is allocable to such interest, over
  o Any amount treated as short-term capital gain under the general rules with respect to the transfer of such interest

• Generally look-through treatment for partnership interests (except for a PTP interest, which is already a specified asset)

• The three-year holding period applies notwithstanding the rules of IRC § 83:
  o Same language as the Senate bill
  o Conference report clarified that this means that the three-year holding period requirement applies to an API regardless of whether the recipient included an amount in income upon acquisition of the API or the recipient made an 83(b) election
Interest expense limitation

• **Removed** IRC § 163(n)

• IRC § 163(j) provision combines elements of House and Senate proposals

• For every business – regardless of form – deduction for business interest limited to:

  \[
  \text{business interest income} + 30\% \text{ of adjusted taxable income (ATI)}
  \]

• **Business interest**: interest paid or accrued on indebtedness allocable to a trade or business

• **Business interest income**: interest included in the gross income and allocable to a trade or business.
  
  o Excludes IRC § 163(d) “investment interest” and “investment income”

• Depreciation and amortization **added back** to ATI only for years beginning **before 2022**

• Certain businesses excluded from IRC § 163(j), including:
  
  o Businesses with average gross receipts of $25M or less (after applying certain aggregation rules)
  o Certain real property trades or businesses that elect out
Interest expense limitation

Application to Pass-Through Entities

- IRC § 163(j) interest limitation applies at the entity level to limit partnership interest expense deductions (interest allowed is part of non-separately stated partnership income or loss)

- Partner adjusted taxable income (ATI) does not include distributive share of partnership income, except for its share of “excess taxable income”

- It appears, but it is not entirely clear, that the interest expense that is allowed at the partnership level and allocated to partners is not retested at the partner level

- Partnership allocates “excess business interest expense” to partners in the year of disallowance (reducing outside basis):
  - Treats the excess as paid or accrued by the partner in succeeding years (unlimited carryforward)
  - Partner allowed to deduct excess business interest expense in succeeding year when allocated excess taxable income from the partnership
  - Outside basis is increased for unused excess business interest expense upon disposal or transfer and unused excess business interest expense does not carryforward further

- Similar rules apply to S corporations
Other relevant provisions

Repeal of technical termination rule
- For partnership taxable years beginning after 12/31/17, partnerships are treated as continuing even if 50% or more of the total capital and profits interests of the partnership is sold or exchanged –
  - No short-year tax returns
  - No restart of partnership asset depreciable lives or acceleration of deferred revenue and 481 adjustments
  - Can no longer make new elections, select new accounting methods without filing Form 3115, or select new IRC § 704(c) methods (acquirers succeed to existing elections and methods)

Expands IRC § 743(d) definition of “substantial built-in loss”
- Inside asset tax basis adjustment now also mandatory if a transferee would be allocated a net loss in excess of $250,000 upon a hypothetical disposition by the partnership of all partnership’s assets
- Applicable to transfers of partnership interests after 12/31/17

Basis limitations on FTC and charitable contribution deductions
- General rule is that a partner’s distributive share of losses and deduction are allowed only to the extent of the partner’s adjusted basis in its partnership interest at the end of the partnership taxable year in which the expenditure occurs
- Final bill subjects a partner’s distributive share of charitable contributions (or basis if gain property) and foreign taxes to this limitation
- Applicable to partnership taxable years beginning after 12/31/17
Effectively Connected Income on the Sale of a Partnership Interest

• Amount treated as effectively connected
  o Gain or loss from the sale or exchange of a partnership interest is effectively connected with a U.S. trade or business to the extent the transferor would have had ECI had the partnership sold all of its assets at fair market value on the date of sale or exchange
  o Applicable to sales or exchanges on or after 11/27/17

• Withholding requirements
  o Transferee of a partnership interest must withhold 10% of the amount realized, absent non-foreign affidavit
  o If the transferee fails to withhold, the partnership is required to deduct and withhold from distributions to transferee
  o Applicable to sales or exchanges after 12/31/17 (was 11/27/17 in prior versions of the bill)

• Provides regulatory authority with respect to the appropriate application of the rule to certain nonrecognition transactions
Polling question 5

Is your organization considering a new business structure to increase after-tax profitability in response to the new tax reform legislation?

• Yes, we are thinking of moving from pass-through to C Corp
• Yes, we are thinking of moving from C Corp to pass-through
• No
• Don’t know/Not applicable
Private wealth considerations
## Changes under Tax Cuts and Jobs Act

### Individual ordinary income tax rates

<table>
<thead>
<tr>
<th>Type of tax</th>
<th>Ordinary income tax rates</th>
<th>Current law for 2018 tax year</th>
<th>Conference Agreement - Tax Cuts and Jobs Act Tax years 2018-2025</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Single</td>
<td>Married couples filing joint</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Ordinary Income Tax Rate</td>
<td>Taxable income over But not more than</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Ordinary Income Tax Rate</td>
<td>Taxable income over But not more than</td>
</tr>
<tr>
<td>Ordinary income tax rates</td>
<td></td>
<td>10%</td>
<td>$9,525 $19,050</td>
</tr>
<tr>
<td></td>
<td></td>
<td>15% $9,525</td>
<td>$38,700 $77,400</td>
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<td></td>
<td>25% $38,700</td>
<td>$93,700 $156,150</td>
</tr>
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<td></td>
<td></td>
<td>28% $93,700</td>
<td>$195,450 $237,950</td>
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<td></td>
<td></td>
<td>33% $195,450</td>
<td>$424,950 $424,950</td>
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<td></td>
<td></td>
<td>35% $424,950</td>
<td>$424,950 $480,050</td>
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<tr>
<td></td>
<td></td>
<td>39.6% $426,700</td>
<td>39.6% $480,050</td>
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<tr>
<td></td>
<td></td>
<td>12% $9,525</td>
<td>$38,700 $77,400</td>
</tr>
<tr>
<td></td>
<td></td>
<td>22% $38,700</td>
<td>$82,500 $165,000</td>
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<td></td>
<td></td>
<td>24% $82,500</td>
<td>$157,500 $315,000</td>
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<td></td>
<td></td>
<td>32% $157,500</td>
<td>$200,000 $400,000</td>
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<td></td>
<td>35% $200,000</td>
<td>$500,000 $600,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>37% $500,000</td>
<td>37% $600,000</td>
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</table>
Changes under Tax Cuts and Jobs Act
Individual income tax rates

<table>
<thead>
<tr>
<th>Type of tax</th>
<th>Current law for 2018 tax year</th>
<th>Conference Agreement - Tax Cuts and Jobs Act Tax years 2018-2025</th>
</tr>
</thead>
</table>
| Passthrough rates                                   | Taxed at individual rates                           | • Provides a deduction equal to 20% of “domestic qualified business income”  
• Adopts an “excess business loss” limitation       |
| Long-term capital gains and qualified dividends top rates | • 20% if earn more than:                             | • Rates remain unchanged  
• Proposed changes not included in final language:  
  • FIFO basis determination  
  • Limiting gain exclusion on sale of a principal residence |
  ○ $426,700 if filing single                        |                                                     |  
  ○ $480,050 if married filing joint (MFJ)         |
| Taxability of qualified tuition reductions          | Excludable from gross income                        | Current law retained, ignoring proposals in House and Senate bills |
| Carried Interest                                    | Taxed as capital gain income                        | Adds holding period requirement of 3 years                        |
| Net Investment Income (NII) Tax                     | 3.8% tax on NII over $200,000 if filing single      | Remains unchanged                                                 |
|                                                    | ($250,000 if MFJ)                                   |  
| Alternative Minimum Tax (AMT)                       | • Parallel tax system requiring taxpayer to pay the higher of the regular tax or AMT  
• Exemption amount of $86,200 with phase-out beginning at $164,100 for MFJ | • Parallel tax system requiring taxpayer to pay the higher of the regular tax or AMT  
• Exemption amount of $109,400 with phase-out beginning at $1 million for MFJ |
## Changes Under Tax Cuts and Jobs Act
### Itemized deductions

<table>
<thead>
<tr>
<th>Provision</th>
<th>Current law for 2018 tax year</th>
<th>Conference Agreement - Tax Cuts and Jobs Act Tax years 2018-2025</th>
</tr>
</thead>
<tbody>
<tr>
<td>Standard Deduction</td>
<td>MFJ $13,000; Single $6,500</td>
<td>MFJ $24,000; Single $12,000</td>
</tr>
<tr>
<td>Medical Expenses</td>
<td>Deductible subject to various AGI limits</td>
<td>• Deductible subject to 7.5% of AGI limitation for 2017 and 2018</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Percentage increases to 10% in 2019</td>
</tr>
<tr>
<td>State, Local, and Foreign Real Property Taxes</td>
<td>Deductible</td>
<td>• Deduction of up to $10k ($5k MFS) for the aggregate of non-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Business:</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• State and local property taxes, and</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• State and local income taxes or sales taxes</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• No deduction for foreign property taxes</td>
</tr>
<tr>
<td>State and Local Income Taxes</td>
<td>Deductible</td>
<td></td>
</tr>
<tr>
<td>Mortgage Interest Deduction</td>
<td>• Deductible on loans for acquisition indebtedness up to $1 million and up to $100,000 for home equity indebtedness • Limited to 2 qualified residences</td>
<td>• Existing mortgages grandfathered</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Generally deductible on new loans up to $750,000 MFJ</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Limited to 2 qualified residences</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• No deduction for home equity loan interest</td>
</tr>
<tr>
<td>Student Loan Interest Deduction</td>
<td>An individual may claim an above-the-line deduction for interest payments on qualified education loans for qualified higher education expenses. The maximum amount of the deduction is $2,500.</td>
<td>Current law retained, ignoring proposals in House and Senate bills</td>
</tr>
<tr>
<td>Charitable Contributions</td>
<td>Deductible subject to various AGI limits</td>
<td>Increased limitation for cash contributions from 50% of AGI to 60% of AGI. All other limits based on AGI remain unchanged.</td>
</tr>
<tr>
<td>Personal Exemption Phase-out (PEP) and Limitation on Itemized Deductions (Pease)</td>
<td>Limitations apply to taxpayers with AGI exceeding certain thresholds</td>
<td>Repealed</td>
</tr>
<tr>
<td>Tax Preparation Fees</td>
<td>Deductible subject to 2% AGI limitation</td>
<td>Repealed</td>
</tr>
<tr>
<td>Unreimbursed Employee Expenses - Moving Expenses</td>
<td>Deductible subject to 2% AGI limitation</td>
<td>Repealed</td>
</tr>
<tr>
<td>Personal Casualty Losses</td>
<td>Deductible subject to 10% of AGI</td>
<td>Repealed except for losses in federally declared disaster areas</td>
</tr>
</tbody>
</table>
How does the Conference Agreement reframe your picture of tax deduction planning?

Consider the implications of the repeal of the following itemized deductions:

• State and local property and income/sales taxes greater than $10,000
  o Generally no tax benefit received by prepaying 2018 state and local income taxes in 2017
• An individual or fiduciary taxpayer who pays a state or local income tax in a taxable year beginning before January 1, 2018 with respect to a state or local income tax imposed for a taxable year beginning after December 31, 2017, will be treated as having made the tax payment on the last day for the taxable year for which the tax is imposed

• Nearly all miscellaneous itemized deductions
  o Analyze the tax benefit of prepaying those items that are potentially no longer deductible for 2018
• Need to be mindful of alternative minimum tax (AMT) implications.
• For those items that would be deductible in 2017 and 2018 (e.g., charitable deductions), analyze which year provides the greater benefit. Consider:
  o What income is being offset
  o Implications of Pease limitation
Polling question 6

What provisions of the Conference Agreement most concern/interest you?

• Changes in tax rates
• Loss of itemized deductions
• Taxability of pass-through income
• Taxability of trusts/estates
• Increase in estate and gift tax exemption amount
• Don’t know/Not applicable
As a general rule, the taxable income of trusts and estates is computed as is the taxable income of individual taxpayers unless there is a special statutory rule to the contrary.

- This includes the applicability of the 20% passthrough deduction to trusts and estates

- Repeal of miscellaneous itemized deductions, using the existing statutory language appears to preclude the deduction of any trust or estate administrative expense
  
  o Important to model the implication of these changes
  
  o Consider their effect on the computation of the income distribution deduction and trust taxable income
Estate, gift and generation-skipping transfer tax planning

**What changes**

- Basic exclusion amount in IRC § 2010(c)(3) of the Code increases from $5 million to $10 million
  - The $10 million amount is indexed for inflation occurring after 2011; thus, for 2018, the exclusion amount will be $11.2 million per person
- The increased exclusion amount sunsets of the end of 2025

**What does not change**

- Estate tax is not repealed
- Top estate, gift and generation-skipping transfer (GST) tax rate remains at 40%
- Unified estate and gift tax regime remains
- Step-up in basis at death is retained

**2017 planning tip**

- Continue to make annual exclusion gifts, but do not pay gift tax
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