WARSHAW BURSTEIN

CLIENT ALERT

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The Newly-Adopted Tax Cuts and Jobs Act: Issues for Business Owners, Investors and Entrepreneurs to Address Now

This Warshaw Burstein Alert highlights provisions in the newly-adopted tax plan that business owners, investors and entrepreneurs need to understand and address. Warshaw Burstein's Corporate, Tax, Real Estate, Trusts and Estates, Matrimonial and Family Law and other teams have been evaluating the changes, and are advising clients on potential impacts and planning responses.

The changes take effect on January 1, 2018, although most of the changes discussed below affecting individual taxpayers will expire as of December 31, 2025 unless extended by Congress. Taxpayers will need to assess the impact of the changes on their business, structure and strategic planning, as well as individual owners, officers and employees. Please contact the persons listed in the margin or your Warshaw Burstein attorney to discuss how the tax law affects you.

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Related Practice Areas

Corporate
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Business Overview

Corporate Tax Rate: The current graduated corporate rate structure (with its top rate of 35%) is replaced with a flat 21% rate beginning January 1, 2018. Additionally, the corporate alternative minimum tax (AMT) is repealed for tax years beginning after December 31, 2017.

Pass-Through Business Income: A time-limited deduction for qualified business income was implemented for owners of pass-through businesses such as sole proprietorships, LLCs and S corporations. Such taxpayers will be entitled to a 20% deduction for business-related income subject to wage limits and exceptions. The deduction generally will not apply to income received from personal service businesses, such as law firms, accounting firms, investment advisory businesses, consulting firms or medical service businesses. The deduction applies to tax years beginning after December 31, 2017, and expires for tax years beginning after December 31, 2025.

Depreciable Property: Investments in qualified depreciable property acquired and placed in service after September 27, 2017 may be expensed and written off entirely in the year acquired. This will be in place for five years (or six years for certain property with a longer production period), with a 20% annual phase-out thereafter.

Interest Expense: The deduction for net interest expense (business interest expense less business interest income) has been retained, and is limited to 30% of adjusted taxable income. Adjusted taxable income is a taxpayer's taxable income disregarding (i) business interest expense or income, (ii) net operating loss carryover, (iii) the new pass-through deduction for business income and (iv) deductions for depreciation, amortization, or depletion. Taxable income will be adjusted for depreciation and amortization for taxable years prior to 2022.

Net Operating Losses: The deduction for net operating losses (NOLs) is limited to 80% of taxable income for losses arising in tax years beginning after December 31, 2017, with no carrybacks and unlimited carryforwards. (Prior law allowed carryback for two years and carryforward for 20 years.)

Like-Kind Exchanges: Like-kind exchanges under Section 1031 of the Internal Revenue Code will be limited to real property that is not held primarily for sale. Personal property will no longer qualify for 1031 tax-deferred treatment (excluding exchanges that are in progress in 2017).

Carried Interest: Carried interest income will remain a capital gain, subject to a longer, three-year holding period (one year under prior law).

International Considerations

Creation of Territorial Tax System: The new law establishes a "territorial" system of taxation, pursuant to which U.S. corporations may deduct dividends received from a "specified" foreign corporation. A one-year holding period applies before a corporation may take this deduction.

Overseas Income*:* For 2017, U.S. shareholders who own at least 10% of the voting shares of a foreign corporation will have all previously untaxed income from such corporation deemed to have been repatriated and mandatorily included in such taxpayer's income. Such income that is attributable to cash or cash equivalents will be taxed at a 15.5% rate while all other income from such corporation (i.e., from equipment or real estate) will be taxed at a rate of 8%. Taxpayers may elect to defer payment of the resulting taxes over an eight-year period, with the first payment due when the taxpayer's final tax payment for 2017 is otherwise due.

Individual Taxpayers

Tax Rates: There are seven tax rates for individuals: 10%, 12%, 22% 24%, 32%, 35% and 37%. The top rate applies to individuals with annual income above $500,000 and to married couples filing jointly with annual income above $600,000.

Standard Deduction: The standard deduction will increase for individual taxpayers to $24,000 for married couples filing jointly, $18,000 for heads of households, and $12,000 for other individuals.

Personal Exemption: The personal exemption ($4,050 for 2017) is repealed, and the withholding rules modified accordingly.

State and Local Tax Deductions: Individuals can take no more than $10,000 in state and local tax (SALT) deductions, which include property taxes and either sales or income taxes.

AMT: The AMT remains in place for individual taxpayers, and the exemption is increased to $70,300 for individuals and $109,400 for married couples filing jointly.

Spousal Support and Business Valuations: Commencing in 2019, spousal support (a.k.a. alimony or spousal maintenance) shall no longer be deductible by the payor spouse or taxable to the recipient spouse. Any agreement signed by the parties or decision rendered by a court prior to January 1, 2019, where spousal support is deductible to the payor spouse and taxable to the recipient spouse shall remain in effect. In addition, the new tax law may affect the valuation of a spouse's business interest. Such valuations play an integral role in a divorce proceeding, and may cause significant change in the equitable distribution awarded to each spouse.

Estate, Gift and Generation-Skipping Transfer Taxes: The estate, gift and generation-skipping transfer tax exemptions have been raised from $5.6 million to approximately $11.2 million (approximately $22.4 million for a married couple) in 2018, and will be indexed for inflation in future years, although the inflation adjustment will be less generous than in prior years. The maximum tax rate remains at 40 percent.

Basis Step-Up for Inherited Assets: The increased tax basis for appreciated assets owned at death, known as "step-up," has been maintained. This enables recipients of most inherited assets to sell the assets with little or no capital gains tax payable.

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This Alert touches on a handful of provisions in the complex and lengthy tax law.[1] Forthcoming guidance, technical corrections and regulations from Treasury and the IRS will shed light on the changes. Warshaw Burstein will continue to review the final legislation and developments, and as circumstances warrant we may issue general updates or more detailed information about specific issues. In the meantime, please contact the persons listed below or your Warshaw Burstein attorney to discuss your situation.

[1] https://www.congress.gov/bill/115th-congress/house-bill/1/text

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