ANDERSEN TAX

HOUSE TAX REFORM PROPOSAL – CORPORATE & BUSINESS

The following chart sets forth some of the provisions affecting corporate and business taxpayers in the House's version of the Tax Cuts and Jobs Act, as approved by the House on November 16, 2017. This chart highlights only some of the key issues and is not intended to address all aspects of the proposed legislation. If you have any questions, please contact your Andersen Tax advisor.

As of November 16, 2017

U.S. CORPORATE AND BUSINESS PROVISIONS		
Provision	**Description of Proposed Change**	**Comments**
C Corporation Income Tax Rates	The regular corporate tax rate would be lowered to a flat 20% rate (personal services corporations would be subject to a flat 25% rate) for tax years beginning after 2017. In order to preserve current tax rates on dividend income, the dividends received deduction (DRD) is reduced to 65% and 50% (from 80% and 70%, respectively).	Corporate taxpayers should focus on accounting method changes to accelerate deductions and defer taxable income for the 2017 tax year.
Individual Income – Tax Rate on Pass-through Business Income	The tax rate on partnership or S corporation business income that flows through to its partners or its shareholders would be reduced as low as 25%, which is more than a third less than the regular maximum individual tax rate of 39.6%. The 25% rate would apply to business income as long as the partner or shareholder is a passive investor in the partnership as determined under the long-standing passive-activity loss rules. If the partner or shareholder is active, then the 25% rate would only apply to 30% of the business income with the remainder 70% taxed at regular tax rates, but the 30% may be increased for capital intensive businesses. Partners or shareholders in service businesses would generally not qualify for any reduced rate. The bill amendments provide for a 9% tax rate in lieu of the 12% rate for the first $75,000 ($37,500 if unmarried and $56,250 for heads of households) in net business taxable income of an active owner earning less than $150,000 in taxable income. As taxable income exceeds $150,000 ($75,000 if unmarried and 112,500 for heads of households), the 9%-rate benefit is phased out at $225,000 of taxable income. This 9% rate is phased in over a five-year period.	REIT ordinary income distributions should also be eligible for the 25% rate. Eligible pass-through businesses should consider accounting method changes to accelerate deductions and defer taxable income for the 2017 tax year.
Alternative Minimum Tax	The corporate alternative minimum tax (AMT) would be eliminated beginning in 2018. If a taxpayer has an AMT credit carryforward, the taxpayer would be able to claim a refund of 50% of the remaining AMT credit carryforward for 2019-2021 and claim a refund of all remaining AMT credits in 2022.	Credits allowed shall not exceed the taxpayer's liability. Corporate entities would need to reevaluate the impact of a finite-lived AMT credit carryforward when assessing the need for a valuation allowance.

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Accounting Methods	Cash Method The bill provides for a $25 million average gross receipts threshold beginning in 2018 (increase from $5 million) for corporations and partnerships with corporate partners for use of the cash method of accounting under Sec. 448. The threshold would be indexed for inflation. The provision would repeal the requirement that such businesses satisfy the requirement for all prior years. UNICAP exemption The same business entities would be exempt from UNICAP for real and personal property acquired or manufactured, even for taxpayers where inventory is a material income producing factor in the business. Long-term Contracts A $25 million average gross receipts threshold would apply for purposes of the exception to the requirement to use the percentage-of-completion accounting method for long-term contracts (increased from $10 million) for tax years beginning in 2018.	The provision may help smaller taxpayers reduce the overall costs and administrative burdens related to tax compliance. The provision would not restrict the ability of taxpayers not subject to Sec. 448 to use the cash method of accounting (i.e., S corporations and partnerships eligible to use the cash method of accounting under present law are not restricted under the bill).
Cost Recovery / Increased Expensing	Expensing of 100% of the cost of new investments in qualified depreciable assets acquired and placed in service after September 27, 2017 and before January 1, 2023. An additional year would be available for certain qualified property with a longer production period. The scope of the qualified asset definition is expanded by the elimination of the requirement that original use of the property begin with the taxpayer. Property would be eligible if it is the taxpayer's first use in a non-related party transaction. Qualified property would not include any property used by a regulated public utility company or in a real property trade or business. The election to use AMT credits in lieu of accelerated depreciation would be repealed. The repeal of the election would be effective for tax years beginning after 2017. The limitation for small business expensing of depreciable assets under Sec. 179 would be increased to $5 million and the phase-out amount would be increased to $20 million effective for tax years beginning after 2017 through tax years beginning before 2023. Additional NOL generated by the proposal would not be able to increase any NOL carryback under the provision.	The effective date of September 27, 2017 is intended to prevent businesses from holding off on making investments while the tax reform process continues. The change with respect to taxpayer's first use (as opposed to new property only) will benefit taxpayers that purchase used or refurbished equipment, as well as lessors with operating leases of such property. The bill would not allow the provision to apply to real property trade or business as a tradeoff for exempting real property trades or businesses from the overall limitation on interest expense to 30% of taxable income.

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Business Interest Expense Deduction Limitation	The deduction for net interest expense for all businesses would be limited to 30% of adjusted taxable income after 2017. The limitation would be applied at the filer level. Exceptions would be provided for small businesses, certain regulated public utilities and real property trades or businesses. Additionally, an exception to the interest limitation would be provided for businesses that paid or accrued interest on floor plan financing indebtedness, but trades or businesses with such indebtedness would not be permitted full expensing. The provision allows for a five-year carry forward of disallowed amounts. The carryover attribute would belong to the business, but additional rules would permit a pass-through entity's unused limitation for the taxable year to be used by its owners. Rules would also limit the carryforward of disallowed interest in the event of an ownership change. An additional limitation would apply to U.S. corporations that are part of an International Financial Reporting Group. Sec. 163(j) would be repealed.	This provision would negatively impact many highly leveraged businesses and in many cases would result in a permanent disallowance of interest expense. Businesses with net interest expense should evaluate how changes to the capital structure would prevent permanent loss of interest deductions.
Net Operating Loss (NOL) Deduction	NOL carryovers would offset only 90% of a taxpayer's taxable income. Generally, all carrybacks would be repealed, and the provision would be effective for losses arising in tax years beginning after 2017. For taxable years beginning in 2017, loss carrybacks would be permitted so long as the loss is not attributable to the increased asset cost recovery deductions. NOLs arising in tax years beginning after 2017 that are carried forward would be increased by an interest factor and carry forward indefinitely.	The provision essentially conforms the regular tax NOL utilization to the current AMT rule limited to only 90% of taxable income. While the reduction of tax rates will negatively impact earnings of companies with net deferred tax assets, the indefinite carryover of post-2017 NOLs may benefit taxpayers that would otherwise have valuation allowances recorded against those federal NOL carryovers.
Like-Kind Exchanges of Real Property	The like-kind exchange rules would be modified to allow for like-kind exchanges with respect to only real property for transfers after 2017. A transition rule would apply to certain like-kind exchanges of personal property not finalized on or before December 31, 2017.	Taxpayers that have deferred tax on the recognition of built-in gains in property will no longer be able to achieve this deferral on personal property.

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Contributions to Capital Included in Gross Income	Gross income of a corporation would include contributions to its capital to the extent the amount of money and the fair market value (FMV) of property contributed to the corporation exceeds the FMV of any stock that is issued in exchange for the contribution. Similar rules would apply to non-corporate entities. The provision would apply to contributions made after the date of enactment.	This provision would repeal Sec. 118, but it would not impact Sec. 351 or Sec. 721 contributions.
Modify Treatment of S Corporation Conversions into C Corporations	The provision would treat distributions from certain terminated S corporations as paid from their accumulated adjustments account and from their earnings and profits on a pro-rata basis. Generally, the rule would apply to an S corporation that revoked its S corporation election within two years of the enactment date and that had the same owners on the enactment date and on the revocation date. Any Sec. 481(a) adjustment would be taken into account ratably over a six-year period.	
Meals and Entertainment Expenses	The provision disallows deductions for entertainment expenses and membership dues relating to such activities or other social purposes. In addition, no deduction would be allowed for transportation fringe benefits, benefits in the form of on-premises athletic facilities, or for certain amenities provided to an employee, except to the extent that such benefits are treated as taxable compensation to an employee (or includible in gross income of a recipient who is not an employee). A 50%-deduction limitation would continue to apply only to expenses for food or beverages and to qualifying business meals under the provision. The provision would be effective for amounts paid or incurred after 2017.	Businesses should consider how these changes would increase costs associated with employee perks and entertainment provided to employees and customers. Businesses should also consider how to track the value of amounts provided to employees and non-employees for purposes of reporting amounts to the recipients.

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Deductions for Executive Compensation	The rules governing the deductibility of excessive compensation paid to covered employees of publicly-held corporation would be modified as follows: 1) The performance-based exception would be eliminated, meaning that all compensation paid during the taxable year in excess of $1 million would not be deductible. 2) The definition of covered employee would include (i) the principal executive officer (PEO) and the principal financial officer (PFO) of the corporation at any time during the taxable year, (ii) the next three highest paid officers (other than the PEO or PFO), and (iii) any person who was a covered employee of the corporation for any taxable year beginning after December 31, 2016, and (iv) any beneficiary of a covered employee receiving benefits as a result of the death of the covered employee. 3) Finally, the definition of a publicly-held corporation would be modified to mean any corporation which is an issuer (as defined in Sec. 3 of the Securities Exchange Act of 1934 (SEA)) of securities which are required to be registered under Sec. 12 of the SEA, or that is required to file reports under Sec. 15(d) of the SEA. 4) Once an employee is treated as a covered employee, any further compensation paid to that person is treated as a payment to a covered employee. Remuneration paid to a covered employee would also include any amounts paid to a person other than the covered employee, including payment after the death of the covered employee.	These changes mean that the compensation deduction for all covered employees for any year in which they are a covered employee and any future year would be limited to $1 million. This would apply to any stock options exercised after December 31, 2017, the vesting of restricted stock or restricted stock units vesting after December 31, 2017, as well as the payment of any deferred compensation after December 31, 2017. If enacted, this provision would have a significant effect on the structure of CEO and top executive pay and may result in a significant tax increase for publicly traded companies with significant payments for CEO and top executive compensation.
Repeal of Rollover of Publicly-Traded Securities Gain into Specialized Small Business Investment Companies (SSBIC)	The special rule permitting gains on publicly traded securities to be rolled over to an SSBIC would be repealed. The provision would be effective for sales after 2017.	
Self-Created Property Not Treated as a Capital Asset	Gain or loss from the disposition of a self-created intangible property would be ordinary in character. The election to treat musical compositions and copyrights in musical works as a capital asset would be retained under an amendment to the bill. Additionally, the special rule treating the transfer of a patent prior to its commercial exploitation as long-term capital gain would be repealed. The provisions would be effective for dispositions of such property after 2017.	Taxpayers contemplating a future disposition of self-created intangibles should consider whether the disposition can be accelerated into 2017 if a built-in gain exists.

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Research or Experimental Expenditures and Software Development Costs	Certain research or experimental expenditures (R&E), including software development costs, would be required to be capitalized and amortized over a five-year period (15 years in the case of expenditures attributable to research conducted outside the United States) for R&E expenditures paid or incurred during taxable years beginning after 2022.	R&E costs and software development costs that are expensed for financial reporting purposes would be capitalized and amortized for tax purposes, resulting in unfavorable book/tax differences.
Other Business Tax Base Broadeners	The Sec. 199 deduction for income attributable to domestic production activities after 2017 would be repealed. Most business credits, other than the research credit and low income housing credit would be repealed (New Markets Tax Credit, the Work Opportunity Tax Credit, the rehabilitation tax credit, the employer-provided child care credit, and the orphan drug credit. Various repeals, modifications and extensions would apply to various energy credits. The deduction for lobbying expenses with respect to legislation before local governmental bodies would be disallowed for amounts paid or incurred after 2017. Immediate deduction for litigation costs advanced by an attorney to a client in contingent-fee litigation until the contingency is resolved would be disallowed. Inflation adjustments, expiration dates and phase-out schedules for various tax credits would be modified; certain oil and gas credits would be repealed and the New Markets Tax Credit would be eliminated. The bill also repeals tax-exempt status and credits for certain bonds. Additional changes are proposed to provisions related to life and property and casualty insurance companies, including an 8% surtax on life insurance income.	

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