Center for Agricultural Law & Taxation

So Many Changes! What Tax Professionals Need to Know for the 2018 Filing Season

January 24, 2018

Instructors

- Kristy Maitre, ksmaitre@iastate.edu
- Kristine Tidgren, ktidgren@iastate.edu

2

Center for Agricultural Law & Taxation

Individual and Employer Issues

3

The Sunset Provision

- The law engages a sunset provision for some, but not all of the tax law changes
- Unless otherwise provided, the sunset provision applies to tax years beginning after Dec. 31, 2017 and before Jan. 1, 2026
- The law in reference to the sunset provision uses the term "suspended" rather than repealed for the term of the eight-years the tax provisions remain in effect
- Thus without future extension of these provisions, the law as we currently apply it in 2017 could become law once again on January 1, 2026, with some exceptions
- But, a lot can happen during that timeframe

WHAT IMPACTS 2017 AND OR 2018?

5

Affordable Care Act (ACA) Individual Healthcare Mandate

- The amount of the individual shared responsibility payment would be reduced to zero effective for months beginning after December 31, 2018
- Therefore, 2018 would be the last year we would engage the penalty issue on an individual basis – not the same for employers
- **The penalty applies in 2017 and 2018**
- Note: The individual mandate remains law

ACA Issues

- ACA: Employer Shared Responsibility (ESR)
- Employers with fewer than 50 workers are not subject to the mandate to cover employees with health insurance
- Employers with between 50 and 99 full-time employees are liable for ESR beginning in tax year 2016
- Employers with at least 100 full-time employees are liable for ESR beginning in tax year 2015

ACA Issues

- ACA: Employer Shared Responsibility Payment
- Employers with at least 50 full-time employees are liable for ESR if one of following conditions exists:
  - The employer does not offer health coverage or offers coverage to fewer than 95 % of its full-time employees and dependents, and at least one of the full-time employees receives a premium tax credit, OR the employer offers health coverage to at least 95 % of its full-time employees and dependents, but at least one full-time employee receives a premium tax credit
  - The second option may occur because employer did not offer coverage to that employee, coverage was unaffordable or coverage did not provide the minimum value

Form 1095 Reporting

- Notice 2018-06 extends the due dates for certain 2017 information reporting requirements for insurers, self-insuring employers, and certain other providers of minimum essential coverage under § 6055 and for applicable large employers under § 6056
- Specifically, this notice extends the due date for: Furnishing to individuals the 2017 Form 1095-B, Health Coverage and
- The 2017 Form 1095-C, Employer-Provided Health Insurance Offer and Coverage, from January 31, 2018, to March 2, 2018

Center for Agricultural Law & Taxation

Medical Expense Deduction Threshold

- For tax years 2017 and 2018:
- The threshold on medical expense deductions is reduced to 7.5% for all taxpayers
- The rule limiting the medical expense deduction for AMT purposes to 7.5% of AGI doesn't apply
- After 2018, the threshold will increase to 10% for all taxpayers for both regular and AMT purposes

Center for Agricultural Law & Taxation

New Withholding Tables and Form W-4

- Employers must implement new withholding tables
- Employers will have a transition period in which they will use the 2017 withholding tables while IRS tests the new tables
- The shift away from personal exemptions and the change in itemized deductions may cause some concern for your clients
- IRS stated on January 11, 2018, that the current Form W-4 could be used to determine new withholding in 2018
- Notice 1036, 2018 withholding tables were issued

Center for Agricultural Law & Taxation

January 11, 2017 – Withholding Tables for 2018 Issued

Notice 1036
(Rev. January 2018)

Department of the Treasury
Internal Revenue Service

Early Release Copies of the 2018 Percentage Method Tables for Income Tax Withholding

Future Developments

For the latest information about developments related to Notice 1036, such as legislation enacted after it was published, go to *IRS.gov/Notice1036*.

2018 Withholding Tables

This notice includes the 2018 Percentage Method Tables for Income Tax Withholding. Employers should implement the 2018 withholding tables as soon as possible, but not later than February 15, 2018. Continue to use the 2017 withholding tables until you implement the 2018 withholding tables.

Percentage Method Tables for Income Tax Withholding

cents to the next higher dollar. For example, $2.30 becomes $2 and $2.50 becomes $3.

Withholding Adjustment for Nonresident Aliens

For 2018, apply the procedure discussed below to figure the amount of income tax to withhold from the wages of nonresident alien employees performing services within the United States.

Note. Nonresident alien students from India and business apprentices from India aren't subject to this procedure.

Instructions. To figure how much income tax to withhold from the wages paid to a nonresident alien employee performing services in the United States, use the following steps.

Step 1. Add to the wages paid to the nonresident alien employee for the payroll period the amount shown in the chart below for the applicable payroll period.

Center for Agricultural Law & Taxation

G **Child Tax Credit** (including additional child tax credit). See Pub. 972, Child Tax Credit, for more information.
- If your total income will be less than $XX,XXX ($XXX,XXX if married), enter "2" for each eligible child; then **less** "1" if you have two to four eligible children or **less** "2" if you have five or more eligible children.
- If your total income will be between $XX,XXX and $XX,XXX ($XXX,XXX and $XXX,XXX if married), enter "1" for each eligible child **G** ______

H Add lines A through G and enter total here. (**Note:** This may be different from the number of exemptions you claim on your tax return.) ► **H** ______

For accuracy, **complete all worksheets that apply.**
- If you plan to **itemize** or **claim adjustments to income** and want to reduce your withholding, see the **Deductions and Adjustments Worksheet** on page 2.
- If you are **single and have more than one job** or are **married and you and your spouse both work** and the combined earnings from all jobs exceed $XX,XXX ($XX,XXX if married), see the **Two-Earners/Multiple Jobs Worksheet** on page 2 to avoid having too little tax withheld.
- If **neither** of the above situations applies, **stop here** and enter the number from line H on line 5 of Form W-4 below.

Separate here and give Form W-4 to your employer. Keep the top part for your records.

Form **W-4** | Department of the Treasury Internal Revenue Service

Employee's Withholding Allowance Certificate

► **Whether you are entitled to claim a certain number of allowances or exemption from withholding is subject to review by the IRS. Your employer may be required to send a copy of this form to the IRS.**

OMB No. 1545-0074 | **2018**

1 Your first name and middle initial | Last name | 2 **Your social security number**

Home address (number and street or rural route) | 3 ☐ Single ☐ Married ☐ Married, but withhold at higher Single rate.
Note: If married, but legally separated, or spouse is a nonresident alien, check the "Single" box.

City or town, state, and ZIP code | 4 **If your last name differs from that shown on your social security card, check here. You must call 1-800-772-1213 for a replacement card.** ► ☐

5 Total number of allowances you are claiming (from line **H** above **or** from the applicable worksheet on page 2) **5**
6 Additional amount, if any, you want withheld from each paycheck . . . . **6** $
7 I claim exemption from withholding for 2018, and I certify that I meet **both** of the following conditions for exemption.
- Last year I had a right to a refund of **all** federal income tax withheld because I had **no** tax liability, **and**
- This year I expect a refund of **all** federal income tax withheld because I expect to have **no** tax liability.

If you meet both conditions, write "Exempt" here . . . . ► **7**

Under penalties of perjury, I declare that I have examined this certificate and, to the best of my knowledge and belief, it is true, correct, and complete.

Employee's signature
(This form is not valid unless you sign it.) ► **Date** ►

8 Employer's name and address (Employer: Complete boxes 8 and 10 only if sending to the IRS.) | 9 Office code (optional) | 10 Employer identification number (EIN)

For Privacy Act and Paperwork Reduction Act Notice, see page 2. Cat. No. 10220Q Form **W-4** (2018)

Center for Agricultural Law & Taxation

April 17, 2018 - Due Date of Return

- File Form 1040 by April 17, 2018
- The due date is April 17, because April 15 is a Sunday and the Emancipation Day holiday in the District of Columbia is observed on April 16—even if taxpayers do not live in the District of Columbia

14

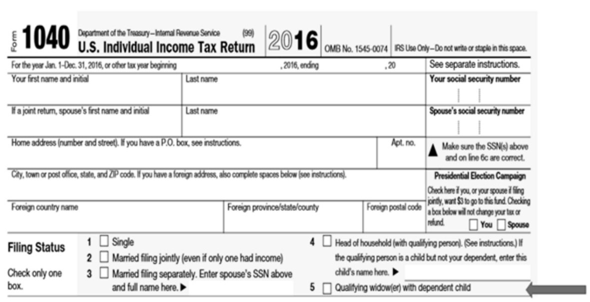
Center for Agricultural Law & Taxation

Tuition and Fees Deduction

- This deduction expired at the end of 2016

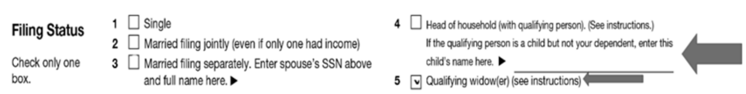
15

Changes in Qualifying Widow or Widower


Form 1040 Department of the Treasury—Internal Revenue Service (99)
U.S. Individual Income Tax Return 2016 OMB No. 1545-0074 IRS Use Only—Do not write or staple in this space.
For the year Jan. 1–Dec. 31, 2016, or other tax year beginning , 2016, ending , 20 See separate instructions.
Your first name and initial | Last name | Your social security number
If a joint return, spouse's first name and initial | Last name | Spouse's social security number
Home address (number and street). If you have a P.O. box, see instructions. | Apt. no. | ▲ Make sure the SSN(s) above and on line 6c are correct.
City, town or post office, state, and ZIP code. If you have a foreign address, also complete spaces below (see instructions). | Presidential Election Campaign
Foreign country name | Foreign province/state/county | Foreign postal code | Check here if you, or your spouse if filing jointly, want $3 to go to this fund. Checking a box below will not change your tax or refund. You Spouse

Filing Status
Check only one box.
1 Single
2 Married filing jointly (even if only one had income)
3 Married filing separately. Enter spouse's SSN above and full name here. ▶
4 Head of household (with qualifying person). (See instructions.) If the qualifying person is a child but not your dependent, enter this child's name here. ▶
5 Qualifying widow(er) with dependent child

2017 Draft


Filing Status
Check only one box.
1 Single
2 Married filing jointly (even if only one had income)
3 Married filing separately. Enter spouse's SSN above and full name here. ▶
4 Head of household (with qualifying person). (See instructions.) If the qualifying person is a child but not your dependent, enter this child's name here. ▶
5 Qualifying widow(er) (see instructions)

16

Changes in Qualifying Widow or Widower

- Instructions have changed based on the 2017 Publication 17
- The tests for a qualifying widow(er)
  - The client is entitled to file a joint return with the spouse for the year the spouse died
  - It doesn't matter whether they actually filed a joint return
  - The spouse died in 2015 or 2016 and the taxpayer didn't remarry before the end of 2017
  - They have a child or stepchild (not a foster child) whom they can claim as a dependent or could claim as a dependent except that, for 2017:

17

Center for Agricultural Law & Taxation

Changes in Qualifying Widow or Widower

- a. The child had gross income of $4,050 or more,
- b. The child filed a joint return, or
- c. The taxpayer could be claimed as a dependent on someone else's return
- <u>If the child isn't claimed as a dependent on Form 1040 or Form 1040A, line 6c, enter the child's name on line 4 of the form the taxpayer is filing</u>
- <u>If you don't enter the name, it will take IRS longer to process the return</u>

18

Center for Agricultural Law & Taxation

Changes in Qualifying Widow or Widower

- This child lived in your home all year, except for temporary absences
- The qualifying child of a Qualifying Widow(er) is a child, stepchild, or adopted child who qualifies as the taxpayer's dependent for the year or would qualify as the taxpayer's dependent except that he or she does not meet the gross income test, or does not meet the joint return test, or except that the taxpayer may be claimed as a dependent by another taxpayer

Forms 1099 Reporting

- The Protecting Americans from Tax Hikes (PATH) Act of 2015 requires Forms 1099-MISC reporting non-employee compensation (NEC) in Box 7 to be filed by January 31 for both paper filing and electronic filing
- If any of Forms 1099-MISC reporting NEC will be filed after the January 31, 2018 due date, the IRS recommends you separate the submission of those Forms 1099-MISC from the submission of any Forms 1099-MISC that do not report NEC
- The IRS may inadvertently treat all Forms 1099-MISC in a combined submission as subject to the § 6721 penalty for failure to file by January 31, even though many of the forms might not be due until February 28 or March 31

Forms 1099

- The Protecting Americans from Tax Hikes (PATH) Act includes a requirement for employers to file their copies of Form W-2 and Form W-3 with the Social Security Administration by the end of January
- An extension of time to file is no longer automatic
- The IRS will only grant extensions for very specific reasons
- Failure to file these forms correctly and timely may result in penalties

Mailing Your Return Changes

- If the taxpayer lives in Connecticut, District of Columbia, Maryland, Pennsylvania, Rhode Island, or West Virginia and they are mailing in the return, they will need to mail it to a different address this year
- Refund - Department of the Treasury, Internal Revenue Service, Ogden, UT 84201-0002
- Payment - Internal Revenue Service, P.O. Box 37910, Hartford, CT 06176-7910

2017 Disaster Issues

- SPECIAL RULE FOR DETERMINING 2017 EARNED INCOME TAX CREDIT AND CHILD TAX CREDIT:
- Taxpayers can use income from 2016 instead of 2017, if 2016 income is more than the 2017 income, to qualify for the Earned Income Tax Credit and the Child Tax Credit
- Taxpayers do not have to itemize to claim the casualty loss
- The taxpayer's standard deduction would be increased by the net disaster loss, including for purposes of calculating whether they are liable for the alternative minimum tax

23

Center for Agricultural Law & Taxation

Example - Mary

- Mary is a single mother to 2 kids and works as a cashier at a local restaurant
- She earns $15,000 a year and received $5,572 from the Earned Income Tax Credit and $1,800 from the Child Tax Credit in 2016
- Following Hurricane Harvey or Irma, Mary’s restaurant was destroyed and she was unemployed for the rest of 2017
- Mary’s 2017 income was reduced to $10,000 a year and she would qualify for $4,010 from the Earned Income Tax Credit and $1,050 from the Child Tax Credit
- Mary’s total tax credit benefit was reduced by $2,312 in 2017
- Under this law, Mary could use her 2016 income to maximize her tax credit benefit and receive the amount she anticipated before the hurricane

24

Center for Agricultural Law & Taxation

How Does it Work - Making the Election?

- You may be able to elect to use the 2016 earned income to figure the EIC if:
- (a) the 2016 earned income is more than the 2017 earned income, and
- (b) the main home was located in one of the Presidentially declared disaster areas eligible for this relief on the specified date
- Pub. 976 has details – but not yet posted
- If you make the election to use your 2016 earned income to figure your EIC, enter “PYEI” and the amount of your 2016 earned income in the space next to line 66a

TAX YEARS 2018-2025

Tax Brackets

- The provision has seven tax brackets, with a top rate of 37 percent (the top rate under present law is 39.6 percent)

	Bracket Beginning Point				
Rate (%)	Married Filing Jointly/Surviving Spouse ($)	Head of Household ($)	Single Individuals ($)	Married Filing Separately ($)	Estates and Trusts ($)
10	0	0	0	0	0
12	19,050	13,600	9,525	9,525	N/A
22	77,400	51,800	38,700	38,700	N/A
24	165,000	82,500	82,500	82,500	2,550
32	315,000	157,500	157,500	157,500	N/A
35	400,000	200,000	200,000	200,000	9,150
37	600,000	500,000	500,000	300,000	12,500

Center for Agricultural Law & Taxation

Tax Brackets – Other Issues

- The tax bracket thresholds are all adjusted for inflation after December 31, 2018
- For tax years 2018–2025, an individuals' taxable income will be subject to the seven new tax brackets
- Each bracket was adjusted by 1- 4% points
- The 2017 current tax rates of 10%, 15%, 25%, 28%, 33%, 35%, 39.6%
- Would be replaced with tax rates of 10%, 12%, 22%, 24%, 32%, 35%, and 37% in 2018
- The tax brackets alone may not be a determining factor of tax savings

Center for Agricultural Law & Taxation

Standard Deduction

- The standard deduction is increased
  - $24,000 for married individuals filing a joint return
  - $18,000 for head-of-household filers
  - $12,000 for all other taxpayers
- The amounts will be adjusted for inflation in tax years beginning after 2018
- The issue of: if one itemizes the other must itemize remains in effect – no change

Center for Agricultural Law & Taxation

Standard Deduction- **2018-** Tax Year (Reminder)

- No changes are made to the current-law regarding the additional standard deduction for the elderly and blind
- If the client is age 65 or older or blind or both, they may increase the standard deduction amount via the annual inflationary adjustments
- An individual is considered to be age 65 if they were 65 on December 31, 2018 or they turned 65 on January 1, 2019
- But note, the amounts increased for the 2018 tax year based on the previous announced inflationary adjustments per Revenue Procedure – 2017-58
- Single or Head of Household and not a surviving spouse the amount will be $1,600
- Married Filing Jointly or Surviving Spouse will be $1,300
- IRS will announce any future inflationary adjustments as required

Center for Agricultural Law & Taxation

Impact on Filing Requirements

- Beginning after December 31, 2017 and ending December 31, 2025 the current filing requirements are changed
  - $24,000 for married individuals filing a joint return
  - $18,000 for head-of-household filers
  - $12,000 for all other taxpayers
- The additional standard deduction remains unchanged by the law except for inflationary adjustments

Center for Agricultural Law & Taxation

Example

- Joe is 70 years old and qualifies for an additional standard deduction
- The basic standard deduction for Joe in 2018 is $12,000
- The additional standard deduction of $1,600 for single individual over 65 or blind or both applies
- Therefore the filing requirement for Joe would be $13,600

Center for Agricultural Law & Taxation

Personal Exemptions

- The deduction for personal exemptions is effectively suspended

Center for Agricultural Law & Taxation

Personal Exemption Special Circumstances

- The personal exemption is used in many corresponding code sections
- To maintain consistency within the code, the dollar amount to be used is $4,150 (2018) when specific provisions contain references to the personal exemption as adjusted by inflation
  - §151(d) personal exemption
  - §642(b)(2)(C) exemption deduction for qualified disability trusts
  - § 3402 wage withholding for 2018
  - § 6334(d) property exempt from levy

Center for Agricultural Law & Taxation

Personal Exemption Special Circumstances

- The suspension of the personal exemption should not alter the operation provisions of the Code which refer to a taxpayer allowed a deduction under §151 – the personal exemption
- Thus, for instance, § 24(a) allows a credit against tax with respect to each qualifying child of the taxpayer for which the taxpayer is allowed a deduction under § 151
- A qualifying child, as defined under §152(c), remains eligible for the credit, even though the personal exemption has been reduced to zero

Center for Agricultural Law & Taxation

Kiddie Tax Changes

- Taxable earned income of a child is taxed under the rates for single individuals
- Taxable net unearned income of a child is taxed based on the brackets applicable to trusts and estates
- Note: Earned taxable income means, the child's taxable income reduced, but not below zero, by the child's net unearned income
- The definition of a child subject to kiddie tax remains unchanged

Center for Agricultural Law & Taxation

Maximum Rates on Capital Gains and Qualified Dividends

- The law generally retains the present-law maximum rates on net capital gain and qualified dividends
- The breakpoints will be indexed for inflation in taxable years beginning after 2017, this would directly effect the breakpoints annually
- Thus, for 2018, the 15-percent breakpoint is
  - $77,200 for joint returns and surviving spouses
  - $51,700 for heads of household
  - $2,600 for estates and trusts
  - $38,600 for other unmarried individuals and married filing separately
- The 20-percent breakpoint is $479,000 for joint returns and surviving spouses
  - $452,400 for heads of household
  - $12,700 for estates and trusts, and
  - $425,800 for other unmarried individuals and married filing separately

Center for Agricultural Law & Taxation

Maximum Rates on Capital Gains and Qualified Dividends

- The capital gains provisions of this law would be effective after December 31, 2017, and sunset after December 31, 2025

Center for Agricultural Law & Taxation

Child Tax Credit

- The child tax credit is increased to $2,000 per qualifying child under the age of 17
- Credit phase out amounts are increased to $400,000 for married taxpayers filing a joint return and $200,000 for all others
- No future adjusted for inflation is provided
- No credit will be allowed to a taxpayer with respect to any qualifying child unless the taxpayer provides the child’s Social Security Number(SSN)

Refundable Portion of the Child Tax Credit

- The amount of the credit that is refundable is increased to $1,400 per qualifying child
- The amount is indexed for inflation, up to the base $2,000 base credit amount
- The earned income threshold for the refundable portion of the credit is decreased from $3,000 to $2,500
- This will result in a larger refundable credit

Partial Credit for Certain Other Dependents

- The Child Tax Credit is modified to temporarily provide for a $500 non-refundable credit for qualifying dependents other than qualifying children and the individual still qualifies as a dependent under § 152
- Examples of how this provision may apply – Regulations will need to clarify:
  - Child over age of 17 - thus the partial credit might apply to a child under 19, a full-time student under age 24, or a disabled child of any age
  - Other qualifying (non-child) relatives if all requirements are met
  - Dependent must be a U.S. citizen, a U.S. national, or a U.S. resident
  - If a qualifying child isn't allowed a CTC because the child doesn't have an SSN that child is treated as a dependent to whom the partial credit applies

Center for Agricultural Law & Taxation

State and Local Tax Deduction Now Limited for Individuals

- State, local, and foreign property taxes, state and local sales taxes and state and local income tax withheld or paid through estimates are deductible This includes the W-2 withholding and estimated tax payments
- An itemized deduction of up to $10,000 ($5,000 for a married taxpayer filing a separate return) for state and local property taxes is allowed
- Foreign real property taxes may not be deducted

Center for Agricultural Law & Taxation

Can Your Client Prepay the State and Local Taxes for 2018 and get a Deduction for 2017?

- No, the law specifically prohibits a taxpayer who, in 2017, pays an income tax that is imposed for a tax year after 2017
- Your client can't claim an itemized deduction in 2017 for that prepaid state and local income tax for 2018

Center for Agricultural Law & Taxation

Exclusion of Gain on Sale of a Principal Residence

- Current law is retained
- A homeowner must live in their home to qualify for the capital gains exclusion for 2 out of the past 5 years
- The exclusion remains at $250,000 single/$500,000 married

Center for Agricultural Law & Taxation

Mortgage & Home Equity Indebtedness Interest Deduction Limited

- The law reduces the limit on deductible mortgage debt to $750,000 for new loans taken out after 12/14/17 - $375,000 for married taxpayers filing separately
- Current loans of up to $1 million are grandfathered and are not subject to the new $750,000 cap
- Neither limit is indexed for inflation
- Homeowners may refinance mortgage debts existing on 12/14/17 up to $1 million and still deduct the interest, as long as the new loan does not exceed the amount of the mortgage being refinanced
- Interest remains deductible on second homes, but subject to the $1 million / $750,000 limits

Binding Contract Issues

- If the client entered into a binding written contract before Dec. 15, 2017 to close on the purchase of a principal residence before Jan. 1, 2018, and the transaction is completed before Apr. 1, 2018, it will be considered to incur acquisition indebtedness prior to Dec. 15, 2017

Mortgage Credit Certificates (MCCs)

- A Mortgage Credit Certificates reduces the amount of federal income tax a client pays each year
- Mortgage Credit Certificates are tax credits
- They reduce the final amount of taxes owed each year
- Current law was retained

Charitable Contribution Deduction Limitation Increased

- The 50% limitation under § 170(b)) for cash contributions to certain public charities and certain private foundations is increased to 60%
- Contributions exceeding the 60% limitation are generally allowed to be carried forward and deducted for up to five years, subject to the later year's ceiling caps

Charitable Contributions - Rules

- A donor who claims a deduction for a charitable contribution must maintain reliable written records regarding the contribution, regardless of the value or amount of such contribution
- No charitable contribution deduction is allowed for a separate contribution of $250 or more unless the donor obtains a contemporaneous written acknowledgement of the contribution from the charity indicating whether the charity provided any good or service (and an estimate of the value of any such good or service) to the taxpayer in consideration for the contribution

Center for Agricultural Law & Taxation

Charitable Contributions- Exception DONEE

- There was an exception to the contemporaneous written acknowledgment requirement for certain contributions reported by the donee organization under §170(f)(8)(D)
- Under the exception, a contemporaneous written acknowledgment is not required if the donee organization filed a return, on such form and includes the same content
- The exception is not available unless and until the Treasury Department and the IRS issue final regulations
- Final regulations were never issued
- The repeal of § 170(f)(8)(D) exception to the contemporaneous written acknowledgment requirement only applies to the donee organization **not the donor**
- Effective date.−The provision is effective for contributions made in taxable years beginning after December 31, 2017

Center for Agricultural Law & Taxation

Simply Stated

- The law repeals the exception to the contemporaneous written acknowledgement requirement for contributions of $250 or more <u>when the donee organization files the required return</u>, effective for contributions made in tax years beginning after Dec. 31, 2016
- Contemporaneous documentation is still required by the donor
- Publication 1771 Charitable Contributions, Substantiation and Disclosure Requirements is a good reference for your clients

College Athletic Seating Rights - No Deduction

- No charitable deduction is allowed for any payment to an institution of higher education in exchange for the right to purchase tickets or seating at an athletic event
- Effective for contributions made in tax years beginning after Dec. 31, 2017

Alimony

- The alimony deduction repeal would affect divorces carried out after December 31, 2018
- If the divorce is later modified after that date and the modification expressly provides that the new amendment will apply to alimony then alimony and separate maintenance payments are <u>not deductible by the payor spouse and are not included in the income of the payee spouse</u>
- The new rule wouldn't affect anyone already paying alimony

Miscellaneous Itemized Deductions Suspended

- The deduction for miscellaneous itemized deductions that are subject to the 2% floor is suspended
  - Expenses for the production or collection of income (investment expenses, etc.)
  - Unreimbursed employee business expenses
  - Unreimbursed vehicle expenses for rural mail carriers
  - Tax determination expenses – fee for preparation of tax return
  - Expenses under the hobby loss rules
  - Repayments of income received under a claim of right (only subject to the 2% floor if less than $3,000)
    - Amount great than $3,000 are not subject to the 2% floor
  - Shares of deductible investment expenses from pass-through entities
- The above list is not all inclusive –ALL deductions subject to the 2% floor are suspended

Phase-out of Itemized Deductions

- This limitation will not apply for tax years 2018-2025

Moving Expenses Deduction Suspended

- No moving expense deduction is allowed
- An exception was created for members of the Armed Forces on active duty who move pursuant to a military order to a permanent change of station

Increase in Individual AMT Exemption and Phaseout Amounts

- The law provides for increased AMT exemptions
- For 2018, the exemptions will be:
  - $109,400 (up from $84,500 in 2017) in the case of a joint return or the return of a surviving spouse
  - $70,300 (up from $54,300 in 2017) in the case of an individual who is unmarried and not a surviving spouse
  - $54,700 (up from $39,375 in 2017) in the case of a married individual filing a separate return

Center for Agricultural Law & Taxation

Increase in Individual AMT Exemption and Phaseout Amounts

- In addition the law would increase the alternative minimum taxable income limit where the exemptions begin to phase out
- The exemption amount of any taxpayer is reduced by an amount equal to 25 % of the amount by which the alternative minimum taxable income of the taxpayer exceeds $1,000,000 (up from $160,900 in 2017) in the case of a joint returns and
- $500,000 for all others (up from amounts ranging from $80,450 to $120,700 in 2017)
- This provision would become effective for tax years after December 31, 2017

Center for Agricultural Law & Taxation

Section 529 Qualified Tuition Programs

- Effective 2018
- 529 plans can allow distributions of up to $10,000 per-student to pay tuition expenses for a public, private, or religious elementary or secondary school
- The rules for postsecondary educational institutions are unchanged

ABLE Account Changes

- Contribution limitations to ABLE accounts made by the designated beneficiary is increased
- Overall the limitation to an ABLE Account is limited to $15,000 (2018 Gift Tax Exemption)
- Once that amount has been reached the ABLE account's designated beneficiary can contribute an additional amount, up to the lesser of :
  - (a) the Federal poverty line for a one-person household; or
  - (b) the individual's compensation for the tax year

ABLE Account Changes

- The ABLE account beneficiary, or a person acting on their behalf, would be responsible for ensuring compliance with the additional contribution limit
- The additional contribution would be not be available if the ABLE account beneficiary made deferral contributions to a 401(k), 403(b), or governmental 457(b) plan
- ABLE account contributions made by the ABLE beneficiary would be eligible for the saver credit

ABLE Accounts and §529 Plans

- For distributions after the date of enactment, amounts from qualified tuition programs (§ 529 accounts) are allowed to be rolled over to an ABLE account without penalty, provided that the ABLE account is owned by the designated beneficiary of that 529 account, or a member of designated beneficiary's family
- Such rolled-over amounts are <u>counted towards</u> the overall limitation on amounts that can be contributed to an ABLE account within a tax year, and any amount rolled over in excess of this limitation is includible in the gross income

Repeal of Special Rule Permitting Recharacterization of IRA Contributions

- Under current law, a Traditional IRA contribution can be recharacterized as a Roth IRA contribution for the same tax year if done by the following October 15 (six-months following the IRA owner's April 15 tax filing deadline)
- The reverse—recharacterizing a Roth IRA contribution to Traditional IRA—can also be done
- IRA owners can also recharacterize the conversion of Traditional IRA assets to a Roth IRA
- <u>The new law eliminates the ability to do a recharacterization</u>

Center for Agricultural Law & Taxation

Repeal of Special Rule Permitting Recharacterization of IRA Contributions

- Recharacterization cannot be done to unwind a Roth conversion
- <u>But</u> an individual may make a contribution for a year to a Roth and before the due date of the return recharacterize it as a contribution to a traditional IRA
- In addition, an individual may still make a contribution to a traditional IRA and convert the traditional IRA to a ROTH but the provision precludes the individual from later unwinding the conversion through a recharacterization

Center for Agricultural Law & Taxation

Taxability of Discharged Student Loan Debt

- Generally, when your client owes a debt and that entity forgives that debt, the amount of the forgiven debt counts as taxable income
- New law in the event of death or total and permanent disability the discharge of student loan debt will no longer be taxable

Center for Agricultural Law & Taxation

Due Diligence Requirements for Claiming Head of Household Enacted

- Effective for tax years beginning after Dec. 31, 2017, the Act expands the due diligence requirements for paid preparers to cover determining eligibility for a taxpayer to file as head of household
- A penalty of $500 (adjusted for inflation) is imposed for each failure to meet these requirements

Center for Agricultural Law & Taxation

Deduction for Personal Casualty & Theft Loss Suspended

- The personal casualty and theft loss deduction is suspended
- Exception: 2018-2025
  - Personal casualty losses incurred in a Federally-declared disaster
  - The losses are subject to:
    - The $100 per casualty adjustment and
    - The 10% of the AGI limitation as with current law is retained in the Federally-declared area

New Exception for Individuals with Casualty Gains – 2018-2025

- When applying the 10%-of-AGI floor to federal disaster losses order matters
  - An individual who has both personal casualty gains and personal casualty losses for a tax year, first must reduce the amount of personal casualty gains by the amount of nonfederal personal casualty losses
  - The remaining personal casualty gains are then used to reduce the amount of the taxpayer's deductible federal disaster losses
  - Any remaining federal disaster losses are deductible to the extent they exceed the 10%-of-AGI floor

New Exception for Individuals with Casualty Gains

- Example: Sally – assume the $100 per event has been taken
- Sally has nonfederal casualty losses $15,000, federal disaster losses of $45,000 and personal casualty gains $20,000 for the tax year with $150,000 of AGI

Example

After applying the $100 per casualty limitation Sally has the following gains and losses

AGI	#1 Nonfederal Casualty Losses	#2 Personal Casualty Gains	#3 Federal Disaster Losses	10% of AGI Adjustment
150,000	15,000	20,000	45,000	
	0 remaining losses	$5,000 gain remaining	$5,000 of gain reduces losses to $40,000	Reduce remaining losses by 10% of AGI or $15,000
				$25,000 deductible federal disaster losses

What About Excess Losses

- Non Federal losses must not exceed gains
  - A taxpayer may deduct the portion of the personal casualty loss not attributable to a federally declared disaster to the extent the loss doesn't exceed the personal casualty gains
  - As far as we know, a federally declared disaster can still create an NOL
  - The NOL would be limited to 80% of taxable income, determined without regard to the NOL itself
  - The three year carry back for casualty and disaster losses has been eliminated
  - The NOL can be carried forward indefinitely

NOL's - Effective for Tax Years Beginning after December 31, 2017

- This effective date means that losses that arose in the tax years prior to January 1, 2018, won't be subject to the 80% taxable income limit
- You will have to distinguish between the two types of NOL's
- Fiscal year taxpayers won't be subject to the 80% of taxable income limitation for the year that began in 2017 and ends in 2018, but will be subject to the limit for the year that begins in 2018

Disaster Area Relief for 2016 Disasters

The new law provides similar relief for any Federally Declared Disaster Area from 2016

Provisions similar to the 2017 disaster relief act include:

- 10% early withdrawal penalty from retirement plans does not apply to qualified 2016 disaster distributions
- Rollover period for qualified 2016 disaster distributions is extended from 60 days to three years
- Income from qualified 2016 disaster distributions is included in income over a 3-year period
- Casualty loss 10% of AGI limit does not apply
- $100 per casualty limit increased to $500, and the deduction can be added to the standard deduction if the taxpayer does not itemize
- Taxpayers can amend prior year returns to take advantage of these provisions

The Disaster Tax Relief Act of 2017 - Review

- Allows special tax breaks for taxpayers affected by Hurricane Harvey, Hurricane Irma, and Hurricane Maria
- Provisions include:
  - 10% early withdrawal penalty from retirement plans does not apply to qualified hurricane distributions
  - Rollover period for qualified hurricane distributions is extended from 60 days to three years
  - Income from qualified hurricane distributions is included in income over a 3-year period
  - Retirement plan withdrawals for home purchases can be re-contributed back into the retirement plan

The Disaster Tax Relief Act of 2017 - Review

- Provisions Continued -
  - Loans from qualified plans can be increased and repayment period extended
  - A new employee retention credit
  - Suspension of limitations on charitable contributions
  - Casualty loss 10% of AGI limit does not apply
  - $100 per casualty limit increased to $500, and the deduction can be added to the standard deduction if the taxpayer does not itemize
  - Earned income for 2017 can be based on 2016 earned income, if less, for purposes of the Child Tax Credit and the Earned Income Credit

Center for Agricultural Law & Taxation

AMT and Disaster Losses

- If an individual has a new disaster loss for any tax year beginning after December 31, 2015 and before January 1, 2018 the AMT adjustment for the standard deduction doesn't apply to the increase in the standard deduction that is attributed to the net disaster loss
- Thus while the standard deduction is generally disallowed under the AMT rules, the portion of the standard deduction attributable to the net disaster loss is ALLOWED for AMT purposes

Center for Agricultural Law & Taxation

Example

- Thomas is a single taxpayer and has a $1,000 net disaster loss
- His standard deduction for 2017 is $6,350
- Therefore that standard deduction for 2017 is increased to $7,350
- When determining AMT Thomas cannot take the standard deduction BUT he can deduction the $1,000 net disaster loss when determining AMT

Additional Disaster Relief for 2016 and 2017 Disasters - Summary

- If an individual has a net disaster loss, the standard deduction is increased by the net disaster loss
- The taxpayer does not need to itemize
- A net disaster loss is defined as the excess of:
  - Qualified disaster related personal casualty losses over personal casualty gains

Gambling Losses

- The limitation on wagering is clarified and modified to provide that all deductions for expenses incurred in carrying out wagering transactions, and not just gambling losses, are limited to the extent of gambling winnings
- This will include travel expenses or fees, to the extent those expenses exceed gambling gains
- Gambling losses remain a Schedule A deduction up to winnings, not subject to the 2% adjustment

Entertainment Expenses - Prior Law

- No deduction is allowed for ordinary and necessary expenses for an activity of a type generally considered to be:
  - Entertainment
  - Amusement
  - Recreation, or
  - For a facility used in connection with such an activity
- Unless the taxpayer established that the expense was "directly related to or associated" with the active conduct of a taxpayer's trade or business or income producing activity
- The deduction could not exceed the portion of the item that met the "directly related to or associated with" standards
- The deduction was generally limited to 50 %

Entertainment Expenses §274 - Prior Law

- In addition, no deduction is allowed for membership dues with respect to any club organized for business, pleasure, recreation, or other social purpose

Entertainment Expenses §274(e)- Prior Law

- There are a number of exceptions to the general rule disallowing deduction of entertainment expenses and the rules limiting deductions to 50 %
- The rules do not apply to
  - Expenses for goods, services, and facilities to the extent that the expenses are reported by the taxpayer as compensation and as wages to an employee
  - Expenses for goods, services, and facilities to the extent that the expenses are includible in the gross income of a recipient who is not an employee (e.g., a nonemployee director) as compensation for services rendered or as a prize or award
- The amount of the deduction cannot exceed the amount of the taxpayer's actual cost, even if a greater amount (i.e., fair market value) is includible in income

Entertainment Expenses §274(e) Prior Law

- Exceptions:
  - Expenses paid or incurred by the taxpayer, in connection with the performance of services for another person (other than an employer), under a reimbursement or other expense allowance arrangement if the taxpayer accounts for the expenses to such person
  - Expenses for recreational, social, or similar activities primarily for the benefit of employees other than certain owners and highly compensated employees
  - The 50% deduction limit for food and beverages for employees on the business premises

Entertainment Expenses §274(e)- Prior Law

- More Exceptions
  - Employee, stockholder business meetings
  - Meetings of business leagues necessary for the attendance
  - Items made available to the public
  - Entertainment sold to customers

Entertainment Expenses – New Law

- Entertainment expenses are completely nondeductible, regardless of whether they are <u>“directly related or associated”</u> with the taxpayer’s business, unless one of the § 274(e) exceptions apply
- § 274(e) was not changed by the new law – we just listed the exception under § 274 (e)

New Law – Entertainment - Summary

- Provisions eliminated
  - The rules that treated a club as an entertainment facility unless it was used primarily to further, and was directly related to the active conduct of, the taxpayer’s trade or business
  - The limit on deductions for tickets to entertainment and sporting events, including the special rules for seats in skyboxes and the special exception for charitable sporting events
  - The 50-percent limit on certain entertainment expense deductions

New Law - Entertainment

- The new law limits these rules beginning in 2018 by barring any deduction for “an activity generally considered to be entertainment, amusement, or recreation” (even if they directly relate to or are associated with the business)
- <u>The 50% deduction for food and beverage expenses incurred with operating their trade or business remains, this is defined in §274 (k), I can find nothing that states this section has been suspended or repealed</u>

Please Note

- Employee business expenses that are not reimbursed and previously deductible on Form 2106 and flowed to Schedule A are no longer allowed
- Planning Issue: Accountable plans become golden

What Did Not Change

- Student loan interest is still an adjustment to income with the maximum of $2,500
- Employer Adoption Assistance Programs remain intact
- Dependent Care Accounts remain intact
- Tuition waivers – remain intact - Employees of educational institutions who receive reduced tuition — or a waiver — for themselves, spouses or dependents are generally not taxed on that income
- Employer paid tuition - is not taxable income for as long as it meets certain conditions and amounts to no more than $5,250 a year
- Credit for the Elderly is retained

Center for Agricultural Law & Taxation

What Did Not Change

- Teachers can still take a $250 deduction for money they spend on certain job-related and classroom expenses
- The 401(K) tax break survived intact
- Electric car buyers tax credit of up to $7,500 survived
- Archer Medical Savings Accounts remain unchanged
- User fee calculation requirements for installment agreements remain unchanged
- Exclusion from gross income of certain amounts received by wrongly incarcerated individuals remains unchanged
- American Opportunity Credit and Lifetime Learning Credit remains unchanged

Center for Agricultural Law & Taxation

Overview of Employee Benefits – What Survived the Chopping Block

- Dependent Care Assistance $5,000 – does not apply to certain highly compensated employees under a program that favors those employees
- Educational Assistance - $5,250
- Employee discounts - Discounts in excess of the amounts allowed under § 132(a)(2) are includible in the employee's taxable income
  - The qualified employee discount exclusion does not apply to property or services provided by a different employer through a reciprocal agreement to provide discounts to employees of the other employer
  - Does not apply to certain highly compensated employees under a program that favors those employees

Center for Agricultural Law & Taxation

Overview of Employee Benefits – What Survived the Chopping Block

- Group term life insurance – Exempt up to $50,000 – Exceptions:
  - Does not apply to S corporation employees who are 2% shareholders
  - Does not apply to certain key employees under a plan that favors those employees
  - Must include in income the cost of group term life insurance beyond $50,000 worth of coverage reduced by any amount the employee pays “Code C”
    - Subject to Social Security and Medicare and at option, income tax withholding
- Health Savings Accounts – Exempt from income up to limits
- No-additional cost services - Does not apply to certain highly compensated employees under a program that favors those employees
- Working condition fringe

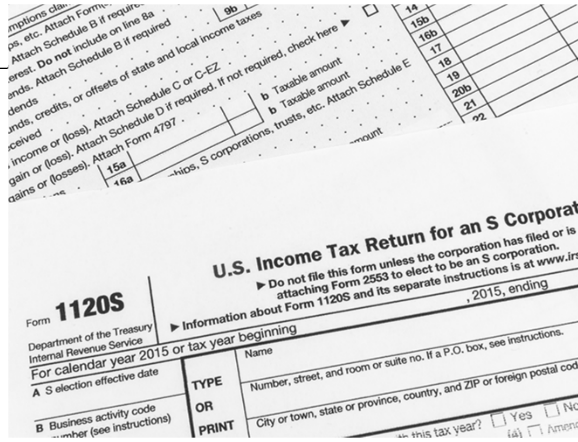
Center for Agricultural Law & Taxation

Saved from Repeal but Still in the Sight of Congress

- Repeal of work opportunity tax credit
- Repeal of deduction for certain unused business credits
  - A provision would have repealed §196 which allows a deduction to the extent that certain portions of the general business credit expire unused after the end of the carryforward period
- Termination of new markets tax credit
- Repeal of credit for expenditures to provide access to disabled individuals
- Modification of credit for portion of employer social security taxes paid with respect to employee tips
- Repeal of exclusion for adoption assistance programs
  - The exclusion from an employee's gross income for qualified adoption expenses paid or reimbursed by an employer would have been repealed

Saved from Repeal but Still in the Sight of Congress

- Liberalization of user fee requirements for installment agreements



Business Issues

95

Center for Agricultural Law & Taxation

CHANGES IMPACTING 2017 RETURNS

96

Center for Agricultural Law & Taxation

Bonus Depreciation

- 100 percent bonus depreciation through 2022, beginning with:
  - Qualifying property acquired *and* placed into service after September 27, 2017
  - Taxpayers can elect to use 50 percent bonus for 2017 purchases.
- Act provides that additional first-year depreciation (bonus) will apply to *used*, as well as new property.

97

Center for Agricultural Law & Taxation

Bonus Depreciation

- Phase-out is as follows:
  - 2023: 80 percent bonus,
  - 2024: 60 percent bonus,
  - 2025: 40 percent bonus, and
  - 2026: 20 percent bonus.
  - After that time, bonus depreciation ends.
- Property acquired before September 28, 2017, but placed in service on or *after* that date, is subject to pre-Act phase-down limits (i.e. 40 percent in 2018).

98

Center for Agricultural Law & Taxation

Section 179

- Beginning in 2018, the Act expanded Section 179 to provide an immediate $1 million deduction (up from $510,000 in 2017) with a $2.5 million phase-out threshold (up from $2,030,000 in 2017).
- These amounts are indexed for inflation beginning in 2019.
- They are permanent.

99

Center for Agricultural Law & Taxation

A Word About State Coupling

- The Act imposes big choices upon states: how will they respond to various provisions
  - Not likely to conform to increased expensing and depreciation options.
    - Iowa still at $25,000 Section 179, $200,000 threshold, no bonus
    - Did not conform to PATH Act provisions like five-year look-back for S Corp to C Corp conversion, educator deduction.
    - Now we will have significant differences.

100

Center for Agricultural Law & Taxation

Like-Kind Exchange

- The Act retained IRC § 1031 like-kind exchange treatment for real property, but eliminated it for personal property, beginning with exchanges occurring after December 31, 2017.
- Elimination of like-kind exchange for personal property is permanent.
- While increased expensing and depreciation options offset impact, there are significant distinctions.

101

Center for Agricultural Law & Taxation

Old Law

- Old law, like kind exchange treatment was mandatory for a trade:
- In 2017, John traded a tractor with a FMV of $75,000 and an adjusted basis of $0 for a tractor with a fair market value of $125,000, plus $50,000 in cash.
  - IRC § 1245 recapture was deferred, and the basis in John's replacement tractor was $50,000 ($0 basis in relinquished tractor, plus boot paid). John could generally use IRC §179 to immediately expense $50,000, the amount of boot paid in the transaction.

102

Center for Agricultural Law & Taxation

New Law

- In 2018, John “trades” a tractor with a FMV of $75,000 and an adjusted basis of $0, plus $50,000 cash for a tractor with a fair market value of $125,000.
- John must now recognize $75,000 in § 1245 recapture. John’s basis in his new tractor will be $125,000, the full purchase price of the new tractor. John can likely use IRC § 179 to expense this amount in 2018. If Section 179 is not available, he can use 100 percent bonus to capitalize and depreciate the full amount in 2018.

103

Center for Agricultural Law & Taxation

What difference does it make?

Same net income in examples, BUT:

- Choosing to apply higher amounts of IRC §179 or bonus depreciation to offset the recognized § 1245 gain will result in lower net Schedule F income, thereby reducing SE income.
  - Planning consideration
- The sale/purchase treatment (as opposed to the like-kind exchange treatment), may be useful in some cases to create ordinary income to offset a net operating loss carryforward.

104

Center for Agricultural Law & Taxation

What difference does it make?

- An accurate trade-in value will now be important.
  - Watching to see if IRS issues regulations governing the reporting of exchanges in light of new law.

105

Center for Agricultural Law & Taxation

2017 Returns

- 100 percent additional first year depreciation is available to qualifying property acquired and placed into service after September 27, 2017. This includes used property.
- Three-month window where 100 percent bonus depreciation and IRC §1031 treatment for like-kind personal property coexist.

106

Center for Agricultural Law & Taxation

2017 Returns

- But, 100 percent bonus applies *only to the boot paid* in such like-kind exchanges.
- IRC § 168(k)(2)(E)(ii) states that property qualifying for bonus depreciation must meet the requirements of IRC § 179(d)(3), which states that "the cost of property does not include so much of the basis of such property as is determined by reference to the basis of other property held at any time by the person acquiring such property."
  - True whether taxpayer elects to take 100 percent bonus or 50 percent bonus, as is available during the first tax year ending after September 27, 2017, under IRC § 168(k)(10).

107

Center for Agricultural Law & Taxation

2017 Returns

- For assets purchased before September 28, 2017, 50 percent bonus would apply to ***both*** the boot and the adjusted basis of the relinquished property, although section 179 could only be used to expense the amount of the boot paid.
- After September 27, 2017, taxpayers may continue to elect *no* bonus depreciation for any class of property. § 168(k)(7).
  - Such election, once made, can be revoked only with the consent of IRS.

108

Center for Agricultural Law & Taxation

State Impact

- Without action by legislature, IRC § 1031 would continue to apply to personal property exchanges for purposes of determining Iowa income.
  - Likely won't couple with bonus and 179 amounts.
- Although Iowa taxpayers can generally expense up to $25,000 and then depreciate an asset acquired in a trade using MACRS, they will likely see significant differences between state and federal taxable income in a year where they must recognize large amounts of IRC § 1245 recapture income because of a trade without § 1031.

109

Center for Agricultural Law & Taxation

Vehicle Depreciation (No Bonus)

The amount of the depreciation deduction for "luxury autos" shall not exceed (for 2018)—

- $10,000 for the 1st taxable year in the recovery period,
- $16,000 for the 2nd taxable year in the recovery period,
- $9,600 for the 3rd taxable year in the recovery period, and
- $5,760 for each succeeding taxable year in the recovery period.

110

Center for Agricultural Law & Taxation

Vehicle Depreciation

- For 2018, the Section 280F(a) depreciation amount for passenger cars and vans and trucks <=6,000 lbs. are the same because adjustments for inflation do not begin until 2019.
  - IRS will again likely apply different inflation adjustment to truck chassis autos.

111

Center for Agricultural Law & Taxation

Bonus and Passenger Vehicles

- The Act *retains the $8,000* limit for additional first-year depreciation for passenger vehicles. But, the law changes bonus to also apply to *used* vehicles.
  - So in first year, taxpayer can deduct $18,000 from passenger auto in 2018.
  - However, further deprecation deductions are not straightforward when bonus is in play.

112

Center for Agricultural Law & Taxation

SUVs and Trucks > 6,000 lbs.

- ***100 percent bonus applies to new or used SUVs and trucks***, for those vehicles purchased and placed in service after September 27, 2017.
- $25,000 Section 179 SUV cap is retained, but with 100% bonus in play, it's not impactful.

113

Center for Agricultural Law & Taxation

Passenger Auto Purchases in 2017

Passenger Cars

- 1st Tax Year $ 3,160 (+8,000)
- 2nd Tax Year $ 5,100
- 3rd Tax Year $ 3,050
- Each Succeeding Year $ 1,875

Light Duty Trucks and Vans

- 1st Tax Year $ 3,560 (+8,000)
- 2nd Tax Year $ 5,700
- 3rd Tax Year $ 3,450
- Each Succeeding Year $2,075

114

Center for Agricultural Law & Taxation

Corporate Income Tax Rate

- *Permanently* lowers the maximum corporate tax rate from 35% to 21%, beginning in 2018.
- Fiscal year C corps apply a blended rate (between old rate and new rate), based upon IRC §15.

115

Center for Agricultural Law & Taxation

NEW DEPRECATION PROVISION

116

Center for Agricultural Law & Taxation

Farm Depreciation

- Beginning in 2018, the Act allows *new* farm equipment to be depreciated over a period of five years, instead of seven years.
- It also removes the requirement that this property is depreciated using the 150 percent declining balance method (except for 15 or 20-year property).
  - These provisions apply to property placed in service after December 31, 2017.

117

Center for Agricultural Law & Taxation

CORPORATE TAX RATE

118

Center for Agricultural Law & Taxation

Corporate Tax Rate – Now a Flat Rate

- Small corporations may consider conversion to S Corporation in light of new law.

Taxable Income	Tax rate (percent)
Not over $50,000	15
Over $50,000 but not over $75,000	25
Over $75,000 but not over $10,000,000	34
Over $10,000,000	35

- Service businesses may consider conversion to C Corporation in light of new law.

119

Center for Agricultural Law & Taxation

NEW IRC § 199A DEDUCTION

120

Center for Agricultural Law & Taxation

New IRC § 199A Deduction

20 percent deduction (subject to many limitations)

- Applies to “qualified business income” received by an individual from a pass-through business:
  - S Corporation
  - Partnership
  - Sole Proprietorship
- Also applies to income from qualified cooperative dividends, real estate investment trusts, and qualified publicly traded partnerships. Calculation for these items is different.

121

Center for Agricultural Law & Taxation

New IRC § 199A Deduction

- Unlike corporate tax rate provision, IRC § 199A deduction is in effect only through 2025.

122

Center for Agricultural Law & Taxation

Qualified Business Income

- The **net** amount of qualified items of income, gain, deduction, and loss with respect to **any qualified trade or business** of the taxpayer. Such term *shall not include any qualified REIT dividends, qualified cooperative dividends, or qualified publicly traded partnership income*.” 199A(c) (the deduction for these items is calculated separately).
- Nor does QBI include wages, reasonable compensation, guaranteed payments, interest income, dividend income, or capital gain. IRC § 199A(e)(4).

123

Center for Agricultural Law & Taxation

Qualified Business Income

- Must be effectively connected with a **U.S.** trade or business.
- There is a separate calculation for each qualified trade or business.
  - Grouping elections apply?

124

Center for Agricultural Law & Taxation

Qualified Business Income = Net Income

Examples:

- Net Schedule F income (minus qualified cooperative dividends)
  - Form 4797 recapture – appears to be gain that fits the definition
- Net Schedule C Income
- Net Schedule E Income
- Capital Gain is *excluded*
  - What about §1231 gain? (seems likely IRS will exclude, but law doesn't so state)

125

Center for Agricultural Law & Taxation

Rental Income

Fits within definition of QBI.

- Must rise to the level of *trade or business.*
  - *Commissioner v. Groetzinger*, *480 U.S. 23* (1987)(conducted for income or profit *and* engaged in with some regularity or continuity)
- Trade or business of *renting* property
  - No requirement for active or material participation.
  - Cash rental income would seem to be included.
  - May be some exclusions for isolated rental arrangements.
  - Self-rentals?

126

Center for Agricultural Law & Taxation

Calculating the QBI Deduction

- Generally, the new 199A deduction for QBI is the **LESSER** of:
  - "Combined qualified business income" (lesser of: 20 percent of QBI *or* wages limitation) OR
  - ***20 percent*** of (taxable income minus net capital gain minus qualified cooperative dividends)
- Wages limitation only applies for taxpayers above income threshold ($157,500, single and $315,000, MFJ)
- "Service businesses" only qualify for deduction if income is below the income threshold (phased in).

127

Center for Agricultural Law & Taxation

Wages Limitation

- Taxpayers with taxable income (not counting the new 199A deduction) exceeding $157,500 (single) or $315,000 (married filing jointly) are subject to a W-2 wages limitation.
  - Above those income amount, the deduction phases out over the next $50,000/$100,000 of income.
- If the wages limitation does not apply, "combined qualified business income" simply equals 20 percent of the taxpayer's QBI.

128

Center for Agricultural Law & Taxation

Income Below Threshold

- Jana, single
- Taxable income = $100,000 ($44,000 wages, $68,000 in QBI, minus $12,000 standard deduction)

199A Deduction =

- Lesser of:
  - .20 * $68,000 = $13,600 OR
  - .20 * $100,000 = $20,000

  = **$13,600**

129

Center for Agricultural Law & Taxation

Income *Above* Threshold

James, single taxpayer (partnership cash rental income, **no** w-2 wages)

- Taxable income = $210,000 ($222,000 in QBI minus $12,000 standard deduction)

199A Deduction = *Lesser* of:

- 20 percent of the taxpayer's QBI OR
- the LARGER of: [50 percent of W-2 wages for the trade or business OR the sum of (25 percent of W-2 wages PLUS 2.5 percent of the unadjusted basis immediately after acquisition of all qualified property)]
- **No Deduction because no W-2 wages** or **qualified property (tangible and depreciable)**

130

Center for Agricultural Law & Taxation

What are W-2 Wages?

- "The amounts described in [IRC § 6051(a)(3), (8)] paid by such person with respect to employment of employees by such person during the calendar year ending during such taxable year."
  - Does not include commodity wages.

131

Center for Agricultural Law & Taxation

"Specified service trade or business"

- *services in the fields of health, law, ~~engineering~~, ~~architecture~~, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services, or any trade or business where the principal asset of such trade or business is the reputation or skill of 1 or more of its employees….*IRC §1202(e)(3)(A)
- Plus: investing and investment management, trading, or dealing in securities …, partnership interests, or commodities…

- No Deduction unless income below income threshold (with phase-out) ($157,500, single and $315,000, MFJ) (phased out over next $50K or $100K)

132

Center for Agricultural Law & Taxation

Example

- Mavis is a single accountant with $80,000 in QBI from her business. She has no other income.
- Because her income is below the $157,500 threshold, Mavis can take a QBI deduction:
  - Lesser of:
    - $16,000 (20 percent of QBI)
    - **$13,600** (20 percent of taxable income)
  - Her taxable income will be $80,000-$12,000-$13,600 = $54,400 (**$2,992** tax savings)

133

Center for Agricultural Law & Taxation

Qualified Cooperative Dividends

- 199A Deduction for Qualified cooperative dividends added at the last hour.
  - Significantly favors sales to cooperatives by members over sales to non-coops or sales by non-members.
    - Extent of discrepancy appears unintentional.

134

Center for Agricultural Law & Taxation

Qualified Cooperative Dividends

- "Any patronage dividend (as defined in section 1388(a), any per-unit retain allocation (as defined in section 1388(f)), and any qualified written notice of allocation (as defined in section 1388(c), or any similar amount received from a [pre-subchapter T organization]." IRC § 199A(e)(4).
- Includes per-unit retains paid in money (PURPIM), as well as traditional patronage dividends. It does ***not*** include nonqualified allocations, which are not included in the member's gross income.
  - Reported in box 3 of 1099-PATR (gross sales)

135

Center for Agricultural Law & Taxation

Qualified Cooperative Dividends

- Calculation of the 199A Deduction for qualified cooperative dividends is much simpler than that for QBI. It is the **lesser** of:
  - 20 percent of qualified cooperative dividends (this will typically be gross sale on 1099-PATR) OR
  - 100 percent of taxable income minus capital gains
- Additionally there is **no** W-2 wages limitation
  - This is likely intentional as a nod to loss of DPAD (IRC §199)

136

Center for Agricultural Law & Taxation

Calculation of Qualified Coop Dividend – Example

- $200K in grain sales (reported as PURPIM)
  - $150K in expenses
- Deduction = lesser of:
  - 20 percent of $200K = $40K OR
  - 100 percent of taxable income = $50K - $12K (standard deduction) = **$38K**
  - **Final taxable income = $38K – $38K = 0**

137

Center for Agricultural Law & Taxation

Qualified Cooperative Dividends

Non Coop

- $200K sales
- $150K expenses

$50K net income

Deduction is lesser of:

20 percent of $50K = $10K OR (2) 20 percent of $50K-$12K = $38K *.20 = **$7,600**

Final Taxable Income = $30,400

Coop Sale by Member

- $200K sales
- $150K expenses

$50K net income

Deduction is lesser of:

20 percent of $200K = $40K OR

100 percent of taxable income = **$38K**

Final Taxable Income = $0

138

Center for Agricultural Law & Taxation

What is ahead?

- It appears that a “fix” will be placed into the final spending bill.
  - Likely more than a technical correction
  - Not sure what language will be submitted
- Senators Thune and Hoeven who sponsored the provision have said that the result was unintentional.

140

Center for Agricultural Law & Taxation

What is ahead?

- USDA issued a statement saying that “the federal tax code should not pick winners and losers in the marketplace. We applaud Congress for acknowledging and moving to correct the disparity, and our expectation is that a solution is forthcoming. USDA stands ready to assist in any way necessary.”
- Best to sit tight and not change business practices in response to this new provision until the dust settles.

141

Center for Agricultural Law & Taxation

Deductions for REIT and PTPs

- 20 percent of dividends from real estate investment trusts and 20 percent of income from publicly traded partnerships
- Limited by 20 percent of taxable income (minus capital gains)
- No requirement that income be U.S. sources
- No wages limitation

142

Center for Agricultural Law & Taxation

OTHER PROVISIONS

143

Net Operating Losses

- Beginning in 2018, the Act eliminates the two-year carryback of net operating losses (five-years for farming businesses), but allows a two-year carryback of net operating losses in the case of certain losses incurred in the trade or business of farming.
- It also limits the net operating loss deduction to 80 percent of taxable income for losses incurred after December 31, 2017.

144

Business Interest Limitation

- Although the Act restricts business interest deductions generally to 30 percent of adjusted gross income (beginning in 2018), those restrictions do not apply to businesses with revenue below $25 million.
- The Act also allows a farming business (as defined in IRC § 263A(e)(4)) and agricultural cooperatives to elect not to be subject to the business interest limitation. Such farming businesses, however, would then be required to use ADS.

145

Center for Agricultural Law & Taxation

Other Provisions

- Expanded Cash Accounting ($25 million gross receipts)
- Eliminated DPAD
- Eliminated corporate AMT, but retained individual AMT (increased exemption amounts and phase-out thresholds)

146

Center for Agricultural Law & Taxation

Estate and Generation Skipping Tax

147

Estate Tax Provisions

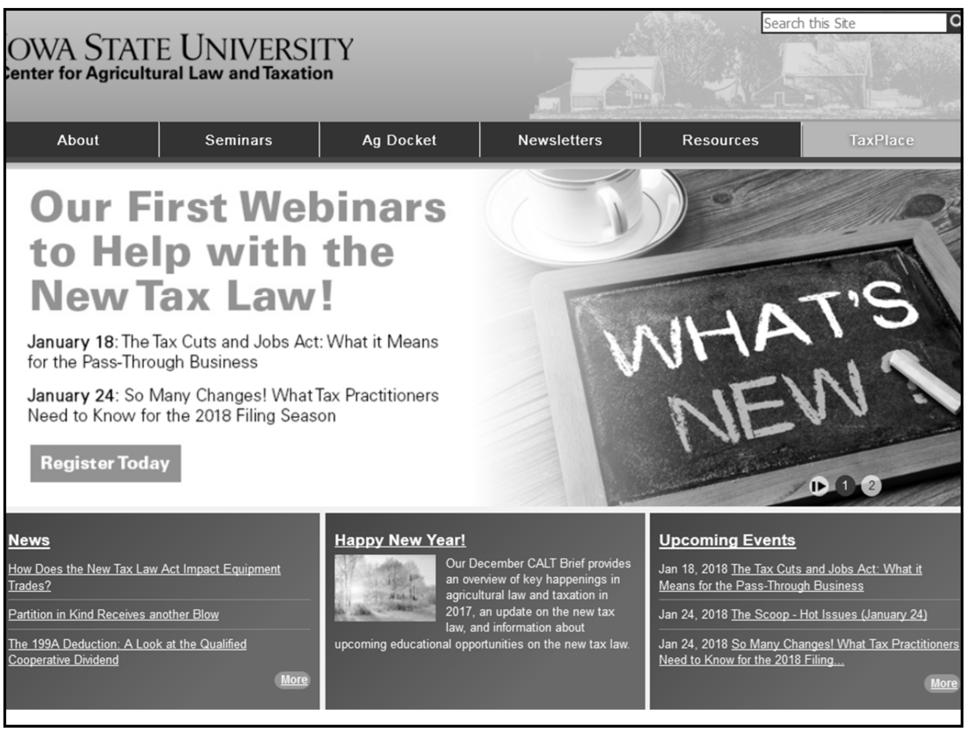
- Doubled the basic exclusion to $11,200,000 per person for estate and gift and generation skipping tax.
  - Gift tax is retained but with 35% maximum and high exclusions.
- Portability Retained
- Basis Adjustment Retained
- **Basic exclusion amounts reset to pre-Act levels in 2026.**

148

CALT Resources

149

Center for Agricultural Law & Taxation



THE AG DOCKET

Perspective on Current Agricultural Law Issues

How Does the New Tax Law Act Impact Equipment Trades?

January 16, 2018
Kristine A. Tidgren

The Tax Cuts and Jobs Act preserved like-kind exchange treatment for real property, but eliminated it for personal property. Today, we take an initial look at what that means for farmers or other taxpayers looking to trade equipment or livestock in 2018. We will soon write separately about vehicle depreciation and trades in light of the new law.

Pre-Tax Cuts and Jobs Act Law

Under 2017 law, IRC § 1031 non-recognition treatment was mandatory for a qualifying exchange of personal property. Those who did not want to apply §1031 like-kind exchange rules to a trade typically had to structure the transaction as a clear sale and purchase to avoid being automatically deemed a like-kind exchange by IRS and the courts. Taxpayers could generally accomplish this by selling the old asset to a different party than the one from whom the new asset was purchased.

With a §1031 exchange, gains or losses on the exchange of like-kind personal property used in a trade or business were generally deferred. This meant that if a farmer traded a fully depreciated piece of equipment for a newer model, the like-kind exchange rules applied, and recognition of IRC § 1245 recapture was deferred. If a farmer traded several raised breeding heifers for some like-kind cows, § 1231 gain would be deferred on that transaction as well. In a like-kind exchange, the basis of the relinquished property was carried over to the basis of the replacement property, and gain recognition was rolled ahead until such time as the replacement property was sold. Specifically, the basis of the replacement property was equal to:

151

Center for Agricultural Law & Taxation

TaxPlace

at the Center for Agricultural Law and Taxation

Subscribe | Replays | Research | Resources | Seminars | CALT

44th Annual Federal Income Tax Schools

Register today to reserve your seat at one of our seven locations throughout Iowa, or attend our **Live Webinar** on Dec. 11-12!

Learn more!

What's New

Minister's Housing Allowance Again Declared Unconstitutional

The Scoop - October 4, 2017

Proposed Valuation Discount Regulations Will Be Withdrawn

More

Check Out Our September Newsletter

Our September CALT Brief summarizes key agricultural law and taxation happenings this month. Read about a new case out of the tax court analyzing SE tax on rent payments to agricultural producers, a review of the latest tax reform proposal, & much more!
Edit Feature

Archive

Upcoming Events

Oct 10, 2017 Webinar: Part 1 - Retirement Planning and Social Security

Oct 11, 2017 Webinar: Part 2 - Retirement Planning and Social Security

Oct 12, 2017 2017 Ag Law Webinars: Iowa Farm Leases - Legal and Tax Considerations

More

Center for Agricultural Law & Taxation

Email tlkayser@iastate.edu

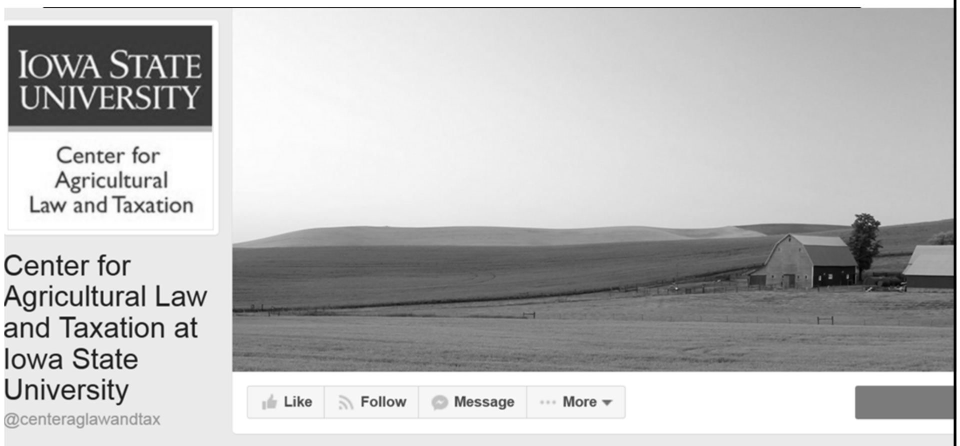
153

Center for Agricultural Law & Taxation

Twitter: @CALT_IowaState

...xation

Facebook: @centeraglawandtax



155

Center for Agricultural Law & Taxation

Questions?

Center for Agricultural Law & Taxation

Kristy Maitre Kristine Tidgren
ksmaitre@iastate.edu ktidgren@iastate.edu
www.calt.iastate.edu
@CALT_IowaState

157

Center for Agricultural Law & Taxation