Lipsitz Green Scime Cambria LLP

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SPECIAL ALERT ON DEVELOPMENTS IN

Tax Reform

What You Should Know About New Tax Legislation

The Tax Cuts and Jobs Act (the "Act") was enacted on December 22, 2017 and drastically changed certain provisions of the Internal Revenue Code of 1986, as amended (the "Code"). The impact of the changes touches practically all businesses and individuals in one way or another. Among other things, the Act permanently decreases the corporate tax rate, temporarily decreases individual income tax rates, limits or eliminates the ability of taxpayers to utilize certain deductions and/or tax credits, includes special provisions allowing certain owners of qualifying "pass-through" businesses and disregarded entities to deduct up to twenty percent (20%) of qualifying business income, and modifies a number of other provisions that will impact businesses and owners going forward. This article briefly summarizes certain provisions of the Act that may be of particular interest to our business clients.

I. Reduction of Corporate Income Tax Rate

Commencing as of January 1, 2018, the corporate tax rate is reduced from a maximum of 35% to a flat rate of 21%. The new flat rate replaces the previous corporate tax system which imposed a graduated rate on corporate income between 15% and 35%. Given the reduction in the corporate tax rate, certain taxpayers may now find it beneficial to organize as a C corporation for tax purposes, depending on the business owner's own tax rates, the availability of utilizing the new deduction of certain income for "pass-through" entities (discussed below), and the unique circumstances of each taxpayer's own situations.

II. Individual Tax Rates and Other Changes Impacting Individual's Federal Income Tax Obligations

Corporations are not the only recipients of reduced tax rates under the Act. Commencing as of January 1, 2018, federal income tax rates for individuals have also been modified, as follows (although the provisions are temporary and will sunset in 2025, absent legislation otherwise):

New Rate (through 2025)	Individuals, Income Over	Married Individuals Filing Joint, Income Over	For Heads of Households, Income Over
10%	$0	$0	$0
12%	$9,525	$19,050	$13,600
22%	$38,700	$77,400	$51,800
24%	$82,500	$165,000	$82,500
32%	$157,500	$315,000	$157,500
35%	$200,000	$400,000	$200,000
37%	$500,000	$600,000	$500,000

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Additional changes imposed by the Act that will impact individuals' federal income tax obligations include, among many others:

- Increase in the standard deduction to $12,000 for single filers and $24,000 for married taxpayers filing jointly.
- Elimination of the individual penalty for individuals that fail to maintain health insurance as mandated under the Patient Protection and Affordable Care Act.
- Elimination and/or limitations on many commonly used deduction and tax credits and, of particular importance in New York, limiting the deduction for state and local income taxes (SALT) to $10,000 (to the extent a taxpayer elects to itemize their deductions).
- Elimination of personal exemptions.

III. New Deduction - Pass-Through and Disregarded Entities

Many businesses are organized as "pass-through" entities for tax purposes, meaning that the entity itself does not pay income tax, but rather the tax attributes of the entity are "passed through" to the business owners, who then pay the applicable tax on their own respective tax return and based on the individual taxpayer's applicable tax rate.

Of particular interest to business owners will be the creation of a new deduction under the Act for owners of "pass-through" businesses or disregarded entities. Determining whether a taxpayer is eligible for the deduction requires a technical analysis of a complicated set of new rules. However, if a taxpayer is eligible, taxpayers that own certain businesses - such as limited liability companies, partnerships, and S corporations - may be eligible to deduct up to twenty percent (20%) of "qualified business income" generated by the "pass-through" entity on the owner's federal income tax return.

There are limitations and restrictions to qualifying for the new deduction. For one, "qualified business income" must be derived from an active trade or business (meaning, income generated from passive investments, such as rental properties, is excluded). Further, income generated by certain service-oriented businesses is excluded from deduction eligibility once a taxpayer's income exceeds a certain threshold amount, and certain compensation paid to an owner, such as compensation paid by an S corporation and guaranteed payments to partners by a partnership, is excluded. Additional limitations based on the unique circumstances of each taxpayer may also apply to limit eligibility for the deduction.

IV. Additional Changes Of Interest to Business Owners

The Act contains a myriad of changes to the Code that will impact businesses and its owners going forward. While a detailed summary of all of these changes is beyond the scope of this article, we believe the following changes will be of particular interest to our clients:

- The elimination of the alternative minimum tax for corporations.
- The elimination of net operating losses ("NOL") carrybacks for most taxpayers. NOLs may still be carried forward to offset income in future years, although the deduction is limited to eighty percent (80%) of taxable income.
- Certain limitations on the ability to deduct business interest expenses incurred by taxpayers.
- Modification of the bonus depreciation rules set forth in Section 168(k) of the Code. Under the Act, taxpayers may deduct one hundred percent (100%) of the cost of property placed in service between the periods of September 28, 2017 and January 1, 2023. Property acquired by taxpayers before September 28, 2017 will continue to be depreciated under the historic bonus depreciation rules of the Code.
- Starting January 1, 2018, the exemption for gift, estate and generation-skipping transfer taxes increases to $10,000,000 per taxpayer, as indexed for inflation.

In sum, passage of the Act has drastically changed the federal tax laws that will impact businesses and individuals, some permanent and others temporarily. Navigating these changes and determining what they may mean for you and for your business can often be difficult. For assistance with this tax reform, or for other corporate inquiries, please contact Lipsitz Green Scime Cambria. The firm's business and corporate attorneys are experienced in a wide variety of corporate issues and work to remain up-to-date on changes that could affect you and your business.

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