

February 5, 2019

Memorandum

To: Our Clients and Friends

From: Bryan J. Morrissey CPA CVA

Subject: **New Tax Law – How It Affects Your Company and You**

As you are most likely aware, in December 2017 President Trump signed into law the **Tax Cuts and Jobs Act of 2017**. This new law is effective primarily for years beginning after December 31, 2017. There are certain changes with an earlier effective date. This memo will focus on the impact on 2018 and beyond.

With an eye towards brevity, the significant law changes are in bullet form below.

- Corporate federal income tax rate reduced from 35% to 21% - *Raising the question of whether or not your company should terminate its Pass-Through status and become a C-Corporation.*
- Pass-through entities (S-Corps., Partnerships, Single-Member LLC's and Self-Employed Individuals), with the exception of certain service companies and others, receive a 20% reduction in the taxable pass through income from their business, thus paying tax on 80% of the business earnings.
- Service Company shareholders, partners, members and proprietors are entitled to the full amount of the pass-through reduction if their taxable income does NOT exceed \$157,500 for single filers and \$315,000 for joint filers. Above this threshold, the deduction is fully phased out at \$207,500 and \$415,000 single/joint.
- Cash Method of Accounting for Income Taxes Increased to \$25MM. *This is a significant change for many of you. The old rule was \$10MM and you may have gone through the painstaking effort to comply with the method change to accrual or percentage of completion. Now, if your revenue is under \$25MM, you may have the option to switch back.*
- Entertainment deductions are eliminated.
- Like-Kind Exchange Rules - now restricted to Real Estate only, no more deferral of gain on traded in equipment and vehicles.
- Net-Operating Losses - May be carried forward only. The old law allowed for a two year carry-back.

- Interest Expense – Business interest deduction is limited to 30% of earnings before interest, taxes, depreciation, and amortization (EBITDA).
- Alternative Minimum Tax is repealed for C-Corporations.
- Section 179 Expense Election - Increased to \$1MM on equipment purchases up to \$2.5MM.
- Bonus Depreciation – Increased to 100% and now includes used equipment.
- State and Local Tax - SALT deduction is limited to \$10,000 - *Impacts the decision as to whether or not operating as a C-Corp. is more beneficial.*
- Mortgage Interest Deduction – New mortgage interest is limited to interest on \$750,000 in acquisition indebtedness.
- Personal Exemptions - Eliminated.
- Standard Deductions - Increased to \$12,000 for Single Filers and \$24,000 for Married Filers.
- New Tax Brackets for All Individual Taxpayers – The new top rate is 37%, down from 39.6%.
- Alimony Deduction – Eliminated for divorces finalized after 2018.
- Estate Tax Exemption – Doubled under the new tax law. *Keep in mind however, that Massachusetts has a \$1MM exemption.*

The above list is not exhaustive, but is directed toward items that have the greatest applicability to you, our clients and friends. Decisions and changes will be made on a client by client basis.

We have run planning models for a certain number of taxpayers. So far, it appears that qualified Pass-through entity owners will benefit from this new tax law, C-Corporations will benefit from this new tax law, but those who own non-qualified pass-through entities (law firms, CPA firms, medical firms, financial service firms and others) and those individuals with significant W-2 income will likely pay higher federal income taxes.

Lastly, the decision to terminate Pass-through status, even though the tax savings may be significant, should not be taken lightly. Other considerations, too numerous to detail here, must be considered.

We are here to help you navigate these law changes. Please feel free to contact us with any questions.