Our Focus on the Tax Cuts and Jobs Act
Thank you for continuing to rely on Marcum for your personal tax and business compliance and consulting needs. We will continue to provide the most knowledgeable and creative planning strategies to assist you in accomplishing your personal and business objectives. Your trust and confidence in us is well-placed.
This 2018 Marcum Tax Guide is unlike any prior year’s. This year we focus on the Tax Cuts and Jobs Act (TCJA) enacted in the waning days of 2017. The TCJA implemented radically new tax provisions affecting both businesses and individuals, with an emphasis on rate reductions, new and complex deductions, and elimination of significant individual itemized deductions. Marcum’s TCJA Advisory Group, led by Michael D’Addio, continues to do an outstanding job analyzing the new tax provisions and providing guidance within the Firm and to our clients and friends. The team’s numerous client alerts, Tax Flashes, memoranda, live presentations, and webinars have been indispensable.

Though the tax law is complex, our TCJA team has focused on enabling our professionals to advise clients how to best take advantage of these new provisions for their businesses and personally. Marcum’s more than 600 tax professionals have mastered the new rules, even as the IRS issues new regulations and guidance. Many important provisions remain unsettled as continuing guidance is issued almost daily. I am extremely proud of our team and know that in the coming months you will seek us out for problem-solving and creative planning strategies.

The new tax provisions include many effective dates and sunset provisions. As we go to press, numerous important tax dates remain fresh in my mind, but as a life-long New York sports fan, one recent sport date reinforces a principle I consider daily as our Firm’s tax leader. On September 25, the captain of our New York Mets, David Wright, was activated so that on September 29 he could play his last professional game. His dedication to his team and sport is an example all of us here at Marcum emulate.

On the tax side, September 28, 2017, was the date when 100% bonus depreciation became effective under the new tax law. Unfortunately, when January 1, 2018 – the effective date for most provisions – rolled around, uncertainty ruled with respect to whether bonus depreciation applied to certain categories of asset additions. This uncertainty remains.

In early summer, the U.S. Supreme Court radically changed the ability of states to collect sales tax, while setting the stage for expansion of their income tax reach through future legislation. Wayfair, decided June 21, 2018, overturned Quill with respect to the physical presence test. States can now require remote sellers to collect sales taxes, even without a physical presence.

Congress is now considering making many of the TCJA individual provisions permanent, enhancing retirement programs, and enacting specified business innovation provisions in what is being called “Tax Reform 2.0.” The timeline for legislation is uncertain, so continue to watch for our Tax Flashes and updates for the latest information.

Last year my message acknowledged the natural disasters affecting many of our fellow citizens in places such as Puerto Rico and Texas. This year our fellow citizens in the Carolinas, the Florida Panhandle and elsewhere are suffering from similar natural disasters. We wish them well, and again, acknowledge that our government is assisting them with both material and legislative relief. Tax filing deadline extensions and specialized tax relief provisions still apply in federally declared disaster areas.

Thank you for continuing to rely on Marcum for your personal tax and business compliance and consulting needs. We will continue to provide the most knowledgeable and creative planning strategies to assist you in accomplishing your personal and business objectives. Your trust and confidence in us is well-placed.

Please use this guide as a mere summary of many of the new rules and planning opportunities. Continue to “Ask Marcum.” We wish you all the best in the New Year.

Joseph J. Perry
National Leader, Tax & Business Services
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About MARCUM LLP

Marcum LLP is one of the largest independent public accounting and advisory services firms in the nation, with offices in major business markets throughout the U.S., as well as Grand Cayman, China and Ireland. Headquartered in New York City, Marcum provides a full spectrum of traditional tax, accounting and assurance services; advisory, valuation and litigation support; and an extensive range of specialty and niche industry practices. The Firm serves both privately held and publicly traded companies, as well as high net worth individuals, private equity funds and hedge funds, with a focus on middle-market companies and closely held family businesses. Marcum is a member of the Marcum Group, an organization providing a comprehensive array of professional services. Established in 1951, Marcum is a leader with an outstanding reputation at the national and regional levels. Marcum is ranked as one of the largest firms in the New York metropolitan area (Crain’s New York Business), the New England region (Boston Business Journal) and the Southeast (South Florida Business Journal).

Marcum offers an extensive range of professional services and a high degree of specialization. In addition to domestic and international tax planning and preparation, the Firm’s professional services include mergers and acquisition planning, family office services, forensic accounting, business valuation and litigation support. The Firm has developed several niche practice areas serving private equity partnerships; hedge funds; SEC registrants; real estate; government, public and not-for-profit sectors; manufacturing; construction; healthcare; and bankruptcies and receiverships; as well as a China specialty practice.

Marcum professionals combine practical knowledge with years of experience to provide a level of understanding and service that is unique among professional service firms. The Firm takes a team approach to every engagement, ensuring the highest degree of technical knowledge, experience and understanding of current issues and regulatory matters. In addition, as a founding member of The Leading Edge Alliance, a worldwide group of large, independent accounting practices, the Firm’s professionals have added access to a wide range of industry and service specialization.

For more information, visit www.marcumllp.com

Marcum is a member of the Marcum Group, a family of organizations providing a comprehensive range of professional services including accounting and advisory, technology solutions, wealth management, and executive and professional recruiting.

These organizations include:
The Tax Cuts and Jobs Act of 2017 (TCJA) makes significant changes to:

1. Individual & Business Taxation
2. Estate & Gift Taxation
3. International Taxation

The Internal Revenue Service and the Treasury Department have provided guidance in some areas of the new law through proposed regulations, notices, press releases, and revenue procedures. However, due to the scope of the new law, many questions remain about its application in specific situations. This article will examine many aspects of the new law and where things stand as of this writing.

**INDIVIDUAL TAXATION**

Rates: The TCJA makes a number of changes to the tax law which impact individuals. Most of these provisions are effective for 2018 and are scheduled to expire after 2025. The House of Representatives recently passed several bills comprising Tax Reform 2.0 which would make many of these individual tax provisions permanent. However, given the current composition of the Senate, these bills are unlikely to pass.

The new law establishes seven income brackets; many of these are reductions of previous rates.

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Many of the new rates apply at different income brackets than the prior rates. For example, the 39.6% bracket applied in 2017 to taxable incomes of $418,400 for single filers and $470,700 for joint filers. In 2018, the top tax rate of 37% rate will apply to taxable incomes of $500,000 for single filers and $600,000 for joint filers. While the maximum rate will apply to fewer taxpayers, it is impossible not to note the significant marriage penalty at this highest tax bracket. Two unmarried individuals living together can make $500,000 of income each before being subject to the top tax bracket, while married taxpayers filing a joint return are subject to the top rate on income over $600,000.

Preferential rates still apply to long-term capital gains and qualified dividends. However, the maximum 20% rate no longer begins at the highest ordinary income bracket for 2018 and later. Under the TCJA, the 20% rate applies for taxpayers with taxable incomes over $425,800 for single filers and $479,000 for joint filers. This is essentially where the 20% rate would have applied under prior law, inflation adjusted.

Simplification and Changes to Deductions: One of the stated goals of the TCJA was simplification of the tax system. However, simplification can have positive or negative consequences, depending on your particular situation. The impact of these rules cannot be generalized and must be determined on an individual basis.
One of the stated goals of the TCJA was simplification of the tax system. However, simplification can have positive or negative consequences, depending on your particular situation.
Standard Deduction and Personal Exemptions: The law increases the standard deduction to $24,000 for joint filers, $18,000 for head of household filers, and $12,000 for single filers. The additional standard deduction for the elderly or disabled is retained. However, the law eliminates the deduction for personal exemptions and dependents.

This increase is expected to reduce the number of taxpayers who itemize deductions. The benefit of the larger standard deduction is offset to some extent by the repeal of personal exemptions. For example, non-itemizing joint filers with two dependents receive an increase in the standard deduction of $11,300 ($24,000 under TCJA vs. $12,700 in 2017), but lose the benefit of four personal exemptions worth $16,200 ($4,050 each). This produces a net increase to taxable income, though the rate reductions may still produce an overall reduction in tax due. If there are no dependent children, then the loss of the personal exemptions is worth $8,100, and there is a net reduction in taxable income. As this illustrates, you cannot determine the impact of the rule changes without applying them to your personal situation.

Other Changes to Popular Itemized Deductions:

▶ State and Local Tax (SALT) Deduction: The itemized deduction for an individual’s state and local income and property tax is now limited to $10,000. This limitation does not apply to deductions related to a trade or business or to investment assets. The change in law primarily affects high-tax states and has spurred these states to attempt to create “work-around legislation.” A common approach by these jurisdictions is to permit a taxpayer to make a contribution to a designated charity in exchange for a tax credit which can be used to offset income or property taxes. This is intended to convert the income tax deduction (potentially limited under the SALT rule) into a charitable contribution deduction. In response, the IRS issued proposed regulations requiring the charitable deduction to be reduced by the amount of any tax credit which exceeds 15% of the total contributed. However, the Service subsequently issued a release stating that a “business-related payment” to charity or government entity does not have to be reduced by an associated tax credit. This has spurred interest in “business-related payments.”

▶ Personal Casualty Losses: A deduction is limited to personal casualty losses resulting from federally declared disasters through 2025.

▶ Mortgage Interest: A deduction remains on mortgage interest related to debt to acquire a primary or secondary residence. However, for acquisition indebtedness in place after December 14, 2017, the deduction is limited to interest on up to $750,000 of debt. For debt in place before December 15, 2017, the existing $1 million limit still applies. Significantly for many taxpayers, the interest deduction on home equity debt not used for acquisition or improvements to the residence is repealed.

▶ Moving Expenses: The moving expense deduction previously allowed in calculating adjusted gross income is disallowed beginning in 2018 (except for members of the armed forces for certain expenses). Employer reimbursements for such expenses will no longer be excluded from employee income. However, the IRS has recently issued guidance that a 2018 employer payment or reimbursement for a 2017 employee moving expense will not be included in the employee’s income. Employers who have treated such payments as employee income for income tax and payroll tax purposes should make corrections per IRS instructions.

▶ Miscellaneous Itemized Deductions: Are no longer allowed. This category of expenses includes tax preparation fees, unreimbursed employee business expenses, repayment of social security benefits, trustee fees for an IRA if billed separately, and repayments of income under a claim of right.

▶ Alimony Payments: Will not be deductible for any divorce decree or separation agreement executed or modified after 2018. The corresponding income inclusion rules for such alimony are eliminated. Payments made under old agreements remain deductible and/or taxable per prior law.

Not all of the changes to deductions affecting individuals are negative. Among the favorable changes are the following:

▶ For 2017 and 2018, the medical expense itemized deduction is allowed for amounts in excess of 7.5% of adjusted gross income for all taxpayers.

▶ The distribution rules for Section 529 education plans are changed so that up to $10,000 of elementary to high school costs annually will constitute qualified costs.

▶ The Pease Limitation, which previously reduced certain itemized deductions for high earners, was repealed. The impact is less significant given the adjustment to itemized deductions discussed above.
The TCJA establishes a new Non-Child Dependent Credit of $500 for a dependent who would not be eligible to be covered under the child tax credit.

**Child Tax and Non-Child Dependent Credits:** The TCJA provides a greater benefit for those eligible for the child tax credit. This credit is increased to $2,000 (versus $1,000 in 2017) per eligible child. Additionally, the law sets higher adjusted gross levels at which the benefit phases out. The refundable portion of the credit is increased from $1,100 to $1,400.

The TCJA establishes a new Non-Child Dependent Credit of $500 for a dependent who would not be eligible to be covered under the child tax credit. This can include children who are 17 or older, or even older dependents. The IRS recently issued guidance which impacts this credit. Generally, a person for whom this credit would be taken cannot have income in excess of the personal exemption amount. Since the personal exemption amount has been reduced to zero, this would make a person with any amount of earnings ineligible. The Service has concluded that in applying this rule, the former personal exemption amount ($4,050 under prior law) should be used.

**Alternative Minimum Tax (AMT):** Despite attempts to eliminate the AMT for individuals, the AMT is still in effect. However, the TCJA increases the exemption amounts used in calculating this tax. In addition, the thresholds at which the exemptions amounts become subject to phase-out are significantly increased. These changes, along with the elimination of miscellaneous itemized deductions and the limitation placed on SALT deductions, will cause many taxpayers who previously were in AMT to no longer be subject to this tax.
BUSINESS TAXATION

The centerpiece of the Tax Cuts and Jobs Act was the changes made to the taxation of business income. The intention of these changes is to spur economic growth through a reduction in business taxation. Highlights of these changes include the following:

C-Corporation Rates and AMT:

- Tax rates for C-corporations are changed from a progressive rate structure of up to 35%, to a flat 21% rate, for tax years beginning after 2017. The special treatment of personal service corporations is eliminated.
- The Alternative Minimum Tax is repealed for businesses for 2018 and later. C-corporations with an AMT credit after 2017 can recover these amounts over a period of up to four years. The AMT credit is available to offset regular income tax, and then 50% of the excess credit is refundable for 2018, 2019, and 2020. Any remaining credit is recovered in 2021.

Qualified Business Income Deduction: Since most business in the United States is not conducted through C-corporations, Congress recognized that it needed to provide relief to businesses which operate as sole proprietors (including single member limited liability companies), partnerships, and S corporations – commonly referred to as “flow-through entities.” The result is a rather complicated set of rules under new section 199A of the Code, under which a 20% deduction is allowed on qualified business income (QBI). A taxpayer in the top 37% tax bracket, after this deduction, pays an effective 29.6% tax on qualified business income. Part of the reason for the complexity under this section of the Code is that while Congress wanted to provide a tax benefit to these businesses, it believed that reduced tax should not extend to amounts received for services.

- For those with taxable income under $315,000 for joint filers and $157,500 for other filers, the 20% deduction applies to all qualified trade or business income.
- For those with taxable income over $415,000 for joint filers and $207,500 for other filers, the 20% deduction applies to qualified trade or business income. However, two separate limitations apply: (i) the deduction is limited to the greater of (a) 50% of W-2 wages or (b) 25% of W-2 wages and 2.5% of the unadjusted basis of investment assets (UBIA) used in the business; and (ii) certain “specified service trades or businesses” do not qualify for the 20% deduction.
- For those with taxable income between the amounts above, a complex set of phase-out rules apply, so that a portion of specified service trade or business income qualifies for the deduction, and the W-2 or W-2/UBIA limits apply in part.

For the Section 199A deduction, “specified services trades and businesses” (SSTBs) includes the field of law, accounting, consulting, financial services, and performing arts; performance of services that consist of investing and investment management trading, dealing in securities, partnership interests, or commodities; and a catch-all provision which includes any trade or business where the principal asset is the reputation or skill of one or more of its employees or owners.

REIT dividends and publicly traded partnership distributive income are eligible for the new 20% deduction, but are not subject to any of the limitations discussed above.

The IRS and Treasury recently issued proposed regulations which provide significant guidance on the operation of the new section 199A deduction, including:

- Determining if the activity constitutes a trade or business.
- Whether businesses can be aggregated for purposes of calculating the limitations on the deduction.
- Defining the meaning of “specified trades and services,” including providing an extremely limited interpretation of businesses falling within the catch-all.
- Banning the “crack-and-pack” strategy. This is where operations or property is pulled from a specified service business (e.g., personnel, IT services, real or personal property rental) and placed into a separate business which then provides the services or leased the property to the related SSTB. The intention is to convert a portion of the SSTB income into income qualifying for the deduction. The proposed regulations treat the related entity as part of the SSTB in whole or part.

However, the proposed regulations provide a number of planning opportunities and considerations:

- The choice of flow-through entity becomes a significant issue. Depending upon whether the limitations apply, an S corporation (which can pay wages to owners) may produce better or worse results than a partnership or a sole proprietorship.
- Partnerships may consider amending agreements to convert guaranteed payments into an allocation of net income, to qualify these amounts for the deduction. The regulations do not require that a partnership make a “reasonable” guaranteed payment to service partners.
- While the typical crack-and-pack strategy is barred, some planning can still be done for separate qualifying businesses from a specified service trade or business, where both provide goods or services to unrelated parties.
A threshold question created by the new law for all businesses is whether they should be conducted in a pass-through form (which has been popular since the Tax Reform Act of 1986) or through a C-corporation. While the corporate tax is reduced to 21%, this decision requires an analysis of a number of other factors, including the double-tax problem when shareholders look to take funds from the C-corporation as dividends or liquidating distributions. Additionally, certain corporations may be limited as to the amounts which can be accumulated under the accumulated earnings tax rules.

**Bonus Depreciation and Section 179 Expense:** All businesses will benefit from the rules increasing the amount of capital costs which can be expensed.

- **Cash Basis:**
  - C-corporations and partnerships with C-corporation partners, and certain farming entities, will be permitted to use the cash basis where average gross receipts for the prior three years is $25 million or less. Previously, the gross receipts level was set at $5 million.
  - Businesses where sales are an income-producing factor are normally required to use the accrual basis with inventories. Prior IRS authority permitted those with average annual gross receipts of $1 million, or $10 million for certain taxpayers, to elect to use the cash basis of accounting. The TCJA increases the threshold to $25 million.
- **Uniform Cost Capitalization:** Businesses, including manufacturers and other producers of property, are exempt from using the uniform cost capitalization rule if they have average gross receipts of $25 million or less.
- **Percentage-of-Completion:** The law’s exception from the use of the percentage-of-completion method for certain long-term contracts to be completed within a two-year period applies to taxpayers with average gross receipts of $25 million or less. This exception permits the use of cash basis or even the completed contract method.

If an election is made to take advantage of an accounting simplification rule, a Form 3115 (Change of Accounting Method) must be filed. The Service has issued guidance indicating that these method changes will be permitted under the automatic change rules. This means that IRS consent is not required.

Use of one of these methods can cause a significant decrease in current year income. However, effective planning must consider the impact of the change over a number of years. Additionally, a number of technical rules must be analyzed to determine that you qualify. Commonly owned businesses may need to be aggregated in determining the level of average gross receipts. Additionally, certain businesses with tax losses and owners who are not active in the business may not be eligible.
TCJA Limits on Certain Business Deductions: The TCJA contains rules which may limit the utilization of the deduction for business interest, net operating loss (NOL) carryovers, and net business losses. Additionally, the deduction for business meals, entertainment, and transportation has been significantly amended.

- **Business Interest Limitation.** Under new IRC section 163(j), every business, regardless of form, is subject to a disallowance of the deduction for net interest expenses (i.e., business interest expense in excess of business interest income) which exceeds 30% of adjusted taxable income. For years beginning before January 1, 2022, adjusted taxable income is business taxable income without considering the deductions for depreciation, amortization, or depletion.

  The law contains several exceptions:

  1. A small business exception excludes a business whose average gross receipts do not exceed $25 million from this limitation. However, as with the accounting simplification rules discussed above, certain commonly controlled businesses will need to be aggregated to determine if this income requirement is satisfied.

  2. Certain businesses can elect out of this interest limitation. They include electing real property trades or businesses or electing farming business. The cost of this election is that the business is required to use the Alternate Depreciation System (ADS) instead of the normal cost recovery rules. ADS requires the use of longer lives and the use of a straight-line method. Of greater significance, those required to use ADS cannot take bonus depreciation on the acquired assets.

  3. Certain floor plan interest is excluded from this rule.

  4. Certain regulated public utilities and electric cooperatives are not subject to this rule.

- **Net Operating Loss Deductions.** The new law repeals net operating loss carrybacks (with a few exceptions) and limits the use of an NOL carryforward to 80% of taxable income of the year to which the loss is carried. However, the carryforward is for an unlimited period. This means that NOLs created in 2018 and later cannot zero the income for a year to which they are carried. Prior NOL carryforwards are not subject to this limit.

- **Non-Corporate Taxpayer Business Loss Limitation.** Net business losses which are allowed against non-business income will be limited to $500,000 for joint filers and $250,000 for other filers. The unused business losses are treated as a net operating loss carryforward to future years. This means that current business losses may not be able offset other current year income. These taxpayers may have taxable income and an income tax obligation, despite incurring real cash losses.

- **Meals and Entertainment.** For amounts paid or incurred after December 31, 2017, business-related entertainment expenses are no longer deductible. Meals while traveling away from home on business remain 50% deductible. A significant change applies the 50% limit to meals provided on the employer’s premises for the convenience of the employer or in an on-premises cafeteria through 2025. In 2026, these amounts will be nondeductible. Entertainment expenses are nondeductible. This includes tickets to a ballgame, a theater performance, or concert.

  Some discussion exists concerning whether business meals survived at the former 50% limit or would be considered nondeductible entertainment. IRS recently issued a Notice confirming that business meals remain 50% deductible with respect to a current or potential business customer, client, consultant, or similar business contact. However, proper documentation should be maintained to establish that this is a business meal and not general entertainment. This includes meals furnished during or at an entertainment facility, so long as they are separately purchased from the entertainment or are separately stated from the cost of the entertainment.

- **Transportation.** Employers cannot deduct the cost of qualified employee transportation benefits (these amounts are nontaxable to the employee). In addition, a deduction is disallowed for the cost of providing any transportation, or any payment or reimbursement, to an employee in connection with travel between the employee’s residence and place of employment, except as necessary for ensuring the safety of the employee. We are waiting for IRS guidance to determine what items are covered under this latter provision.

  Businesses should project their expected operating results to determine the potential application of these rules. These limitations can produce substantial cash flow issues.

  Meals and entertainment costs should be reviewed to determine which are deductible under the new law. Deductible amounts, along with appropriate documentation, should be properly recorded so they are treated correctly on the income tax return.

- **Like-Kind Exchanges.** Due to the increase in bonus depreciation and section 179 expense election discussed above, Congress felt that changes to the section 1031 like-kind exchange rules were appropriate. After 2017, the like-kind exchange rules, which defer recognition of gain or loss on the swap of like-kind property, only apply to real property.
Employers cannot deduct the cost of qualified employee transportation benefits (these amounts are nontaxable to the employee).
QUALIFIED OPPORTUNITY ZONES
The TCJA creates a new investment vehicle which has a tax advantage. For a taxpayer who sells appreciated assets, tax on the gain can be deferred by investing the gain, within 180 days of the sale, in a qualified opportunity fund. The deferral of the gain runs until the earlier of the date the investment in the fund is sold or December 31, 2026. If the investment is held for five years, the amount of gain taxed is reduced by 10%. If the investment is held for seven years, the taxable gain is reduced by 15%. Tax on any additional gain on the investment, if held for 10 years, can be completely eliminated.

The investment vehicle can be organized as a corporation or partnership and must hold at least 90% of its assets in qualified opportunity zones. As of this writing, all states have designated communities which qualify.

ESTATE AND GIFT TAXES
Despite the push to eliminate the “death tax,” the final bill retained the estate and gift tax. However, for 2018 through 2025, the basic exclusion amount for each person is increased to $11,180,000 (about twice the previous amount). A comparable increase applies to the generation tax exemption.

There was some discussion that the law might eliminate the “date-of-death basis rule,” whereby property included in a decedent’s taxable estate receives a tax basis equal to its fair market value on date of death. Consideration was given to a carryover basis approach and to a gains tax. However, the date-of-death basis rule remains the law.

This increase in the exemption will make many estates non-taxable. For these persons, income tax planning involving the date-of-death basis rule may be of greater significance.

Those with large estates may look to leverage the higher basic exclusion amount so as to transfer more asset appreciation out of their estates.

The basic exclusion is scheduled to revert back to the former $5 million dollar level, inflation-adjusted, after 2025. It is not clear that this will ever happen. However, planning must take into account the possibility of reversion.
INTERNATIONAL TAXATION

▸ **100% Dividend Exclusion:** C-corporate shareholders are allowed a 100% deduction for the foreign-source portion of dividends received by a U.S. corporate shareholder from specified 10%-owned foreign corporations. Since the distribution is not taxable, neither a foreign tax credit nor deduction is allowed for foreign income taxes related to a qualifying dividend. This exclusion does not apply to non-corporate taxpayers.

▸ **Section 965 Deemed Repatriation:** A U.S. shareholder in a Deferred Foreign Income Corporation is required to include its pro rata share of the undistributed, non-previously taxed post-1986 foreign earnings. This deemed repatriation applies based on the year-end of the foreign corporation. Many taxpayers dealt with this tax in 2017. However, an inclusion may apply in 2018 for fiscal year foreign corporations. The intention of the law is to produce a 15.5% tax rate on the portion of foreign earnings and profits held in cash and an 8% tax on the balance. However, this is actually done through the mechanism of a deduction allowed with respect to the included income, based on an assumed 35% tax rate.

The resulting tax (“transition tax”) can be elected to be paid over an 8-year period in installments of 8% of the net tax liability for five years, 15% in year 6, 20% in year 7, and 25% in year 8. Shareholders of S corporations which hold interests in a foreign corporation are permitted a special election to defer the tax until certain “triggering events.”

The Service has a Frequently Asked Questions (FAQ) section on its website dealing with section 965 issues. Proposed regulations have also been issued. The Service recently issued a legal counsel opinion stating that an overpayment in a year for which there was a deemed repatriation could not be applied as a credit to a future year’s income tax or be refunded, but must be applied against the unpaid balance of the transition tax, despite the election to pay the tax in installments.

▸ **Global Intangible Low Tax Income (GILTI):** The law has a new inclusion into income of the amount by which “tested income” of foreign affiliates exceeds 10% of such entity’s basis in tangible overseas capital investment used in the business. This is intended to prevent companies from using foreign entities to hold and use intangible property. For 2018 through 2025, corporations can claim a deduction for 50% of the GILTI inclusion. The deduction decreases to 37.5% thereafter. However, this deduction does not apply to non-corporate taxpayers.

The Service has issued proposed regulations on the computation of the GILTI inclusion, but it does not address the interaction with the foreign tax credit.

▸ **Base Erosion Alternative Minimum Tax (BEAT):** This is an alternative minimum tax of 10% (12.5% after 2025) on modified taxable income determined by disallowing the deduction of payments to certain related foreign parties.

It is unclear whether the GILTI and BEAT will survive challenge by the World Trade Organization. The GILTI can be argued to be an improper subsidy. The denial of deductions under BEAT can be viewed as selective tariffs.

ACTION STEPS

This has been a brief description of the most significant parts of the new Tax Act. There are many ways that this new law can impact your personal and business taxes. While analysis will evolve as the IRS issues additional clarification and explanations of the law, the tax professionals at Marcum suggest immediately beginning a review of how these new rules may affect you or your business personally.
Taxpayers who have acquired, or are acquiring, real estate for business use should consider having a cost segregation study performed.
BUSINESS OWNERS FACE OPPORTUNITIES AND CHALLENGES IN ORDER TO COMPLY WITH THE NEW ACT.

As the year concludes, business owners are faced with the opportunity and challenge of evaluating their current year operations and future expectations to determine how to best take advantage or minimize the downside of the numerous changes in tax law taking effect as a result of the Tax Cut and Jobs Act (or “TCJA” or “the Act”). While there have been many updates for the 2018 tax year, the uncertainty as to the interpretation of many of the provisions of TCJA requires business owners and their tax advisors to remain vigilant and up-to-date in order to ensure compliance and the maximization of tax benefits.

Business owners should consider the following tax planning tips based on the tax provisions modified as a result of TCJA and those provisions in place prior to the Act.

- TCJA reduces the C-corporation tax rate to a flat 21% for tax years beginning after December 31, 2017. (The 21% rate will be prorated for fiscal year filers). Taxpayers may consider converting their pass-through entities to C-corporation structure to take advantage of the decreased corporate tax rate.

- TCJA repeals the corporate alternative minimum tax (AMT) for tax years beginning after December 31, 2017, and continues to allow the prior year minimum tax credit to offset the taxpayer’s regular tax liability. For tax years beginning after 2017, and before 2022, the prior year minimum tax credit carryover is refundable. Corporations with prior-year minimum tax credits should consider adjusting their 2018 fourth quarter estimated payments or extension payments to account for these amounts.

- Bonus depreciation has been extended and will now allow a 100% deduction for property acquired and placed into service after September 27, 2017. The definition of qualified property has been also been expanded to include purchased used property. Taxpayers are currently able to elect to deduct as an expense, rather than depreciate the cost of, certain new or used business assets placed in service during the year.

- Taxpayers who have acquired, or are acquiring, real estate for business use should consider having a cost segregation study performed. Generally, property placed in service after September 27, 2017, with a class life of 20 years or less will be eligible for 100% bonus depreciation, whereas non-residential property is usually characterized as 39-year property not eligible for bonus depreciation. A cost segregation study can assist real estate owners in allocating the proper costs of acquisitions among the proper class lives, so that depreciation can be expedited on certain assets.

- The de minimis safe harbor repair threshold remains at $2,500 for most taxpayers and $5,000 for taxpayers with applicable (i.e., audited) financial statements. Under this safe harbor, eligible taxpayers may deduct as an expense, rather than depreciate, the cost of qualified property acquired or repaired.

- The Research and Development Tax Credit is permanent and allows businesses engaging in certain research activities and incurring qualified research expenses to receive a tax credit to offset federal business tax liability and, in the case of a pass-through entity, to offset personal tax liability. Qualified small businesses may also still elect to utilize the credit against FICA payroll taxes.

- Taxpayers with average annual gross receipts of $25 million or less for the prior three taxable years are now permitted to use the cash method of accounting, are exempt from the inventory uniform capitalization (UNICAP) rules, and are exempt from the requirement to use the percentage-of-completion accounting method for long-term construction contracts to be completed within two years. Previously, the average gross receipts threshold was $10 million.

- Cash basis taxpayers may accelerate deductions by prepaying certain expenses before year-end. Also, credit card charges incurred before year-end may be deducted in 2018 and paid in 2019.
Cash basis taxpayers should consider deferring income to 2019 as long as the income is not actually or constructively received.

Accrual basis taxpayers may generally deduct cash payments made within 2 ½ months after year-end for compensation, bonus, and long-term incentive plans.

Under TCJA, a deduction is no longer allowed for entertainment, amusement, or recreation; membership dues for a club organized for business, pleasure, recreation, or other social purposes; or a facility used in connection with any of the above. The deduction for 50% of food and beverage expenses associated with operating a trade or business generally is retained. The Act now limits to 50% employer expenses associated with providing food and beverages to employees through an eating facility meeting de minimis fringe requirements. Taxpayers should review these updates as a result of TCJA to analyze and possibly decrease their entertainment budgets in favor of other expenses that will be deductible.

TCJA disallows deductions for expenses associated with providing any qualified transportation fringe to employees and, except for ensuring employee safety, any expense incurred for providing transportation (or any payment or reimbursement) for commuting between the employee’s residence and place of employment. These amendments generally apply to amounts paid or incurred after December 31, 2017.

Individual owners of pass-through entities should review and determine if there is sufficient tax basis to deduct 2018 business losses at the individual level. Also, it is important to review if there are any tax implications from distributions taken by owners of pass-through entities in 2018. Action should be taken before year-end if additional tax basis is necessary for losses or distributions.

Individual owners of pass-through entities should also take into account that the IRS now disallows an excess business loss which becomes part of the taxpayer’s net operating loss carryover to the following year. An excess business loss for the tax year is the excess of the taxpayer’s aggregate deductions attributable to the taxpayer’s trades or businesses, over the sum of aggregate gross income or gain of the taxpayer plus a threshold amount ($500,000 for married taxpayers filing jointly and $250,000 for all other taxpayers, indexed for inflation). If a taxpayer is planning to offset other earnings with business losses, the taxpayer must consider that potentially only a portion of these business losses will be utilized in the current year.

Taxpayers may still consider various deferral techniques such as installment sales and like-kind exchanges, but it is important to note that the Act now limits the non-recognition of gain or loss to like-kind exchanges of real property that is not held primarily for sale. This amendment generally applies to exchanges completed after December 31, 2017.

Taxpayers should review tax-attribute carryovers, such as net operating losses, capital losses, tax credits, and charitable contributions to determine if there are any expiring carryovers and to what extent carryovers can or should be used in 2018. The NOL deduction limit for NOLs arising in 2018 is now 80% of taxable income, computed without regard to the NOL deduction, and provides that amounts carried over to later tax years are adjusted to take into account this limitation. TCJA also eliminates NOL carrybacks and allows unused NOLs to be carried forward indefinitely.

Individual taxpayers that use a portion of their homes for business purposes should consider deducting expenses incurred for that portion of the home. The deduction is limited to business income; however, disallowed expenses may carry forward to future years.

For tax years beginning after December 31, 2017, and before January 1, 2026, taxpayers who have domestic “qualified business income” (QBI) from a partnership, S corporation, or sole proprietorship are entitled to a deduction equal to: (1) the lesser of the combined qualified business income amount of the taxpayer or 20% of taxable income (reduced by net capital gain), plus (2) the lesser of 20% of qualified cooperative dividends or taxable income (reduced by net capital gain). The deduction reduces taxable income, not adjusted gross income, and eligible taxpayers are entitled to the deduction whether or not they itemize. Shareholders of businesses operating as S-corporations should first determine their eligibility for the 20% QBI deduction and then review year-end compensation to distribute business profits, as well as meet 2018 estimated tax requirements through final income tax withholdings.
The Act limits the deduction for net interest expense incurred by a business to the sum of business interest income, 30% of adjusted taxable income, and floor plan financing interest. Businesses with average annual gross receipts of $25 million or less are exempt from this limitation. Disallowed interest may be carried forward indefinitely. Taxpayers should take into account interest expense limitations post-TJCA when deciding between equity and debt financing.

The Act provides a 100% deduction for the foreign-source portion of dividends received from “specified 10-percent owned foreign corporations” by U.S. corporate shareholders, subject to a one-year holding period. Corporations are no longer required to keep foreign earnings offshore and should repatriate cash as they deem necessary to support business operations.

**ACTION STEPS**

As year-end approaches, it is important for business owners and individual taxpayers to be in touch with their tax advisors. The 2018 tax year will be the first time many of the new provisions from TCJA will be implemented, and there are myriad tax decisions that must be considered.

While this planning guide reflects many action items to review prior to year-end, below is a short list of items to consider:

1. Review whether converting to another entity type will provide an overall tax benefit.
2. Review opportunities to elect 100% bonus depreciation.
3. Review tax basis in pass-through entities and total estimated business losses to determine whether 2018 business losses will be deductible.
4. Review compensation amounts to minimize the effective tax rate.
5. Evaluate whether foreign cash should be repatriated to support onshore business operations.
An Expanded Universe for Small Business Taxpayers

THE NEW TAX ACT OFFERS MANY FAVORABLE REFORMS TO SMALL BUSINESS OWNERS INCLUDING DROP IN RATES AND ACCELERATED DEPRECIATION.

The Tax Cuts and Jobs Act (TCJA or “the Act”) of 2017 provides many favorable tax reforms for businesses. Among these reforms is an increase in the small business taxpayer gross receipts threshold from $5 million (or $10 million in certain cases) to $25 million. Previously, taxpayers that surpassed the $5 million ($10 million) gross receipts threshold were required to use accrual basis accounting, Section 263A inventory capitalization, percentage-of-completion method for long-term contracts, and account for inventories. The increased threshold under the TCJA offers relief to more small business taxpayers with respect to accounting method reform and simplification. The TCJA references the existing gross receipts test under section 448(c) of the Internal Revenue Code (IRC or “Code”) when determining whether a taxpayer qualifies as a small business taxpayer. However, the TCJA made two modifications to the existing test. First, the gross receipts threshold was increased from $5 million (not adjusted for inflation) to $25 million (adjusted for inflation), and second, the averaging period was changed from all prior years to the three prior taxable years.

It is also important to note that when calculating average gross receipts for these purposes, businesses are subject to the aggregation rules. Under the aggregation rules, the gross receipts from multiple businesses must be aggregated where they meet either a “controlled group” ownership test or an affiliated service group (ASG) test.

This article provides an overview of the simplified accounting method provisions for small business taxpayers under the TCJA, as well as one modified accounting method provision that applies to all accrual basis taxpayers. In addition, it outlines possible benefits and consequences of each accounting method change as well as the effective dates for the changes.

EXPANDED USE OF THE OVERALL CASH METHOD OF ACCOUNTING FOR SMALL BUSINESS TAXPAYERS

Before TCJA: Under Section 448 of the Code, C-corporations and partnerships with corporate partners were prohibited from using the cash method of accounting for tax purposes unless their average annual gross receipts were $5 million or less for the average of the three prior years.

After TCJA: The threshold for average gross receipts increased from $5 million to $25 million and is calculated by averaging the taxpayer’s gross receipts for the three prior taxable years. Effective for years beginning after December 31, 2017, the cash method of accounting may be used by taxpayers, other than tax shelters, that satisfy the $25 million gross receipts test, regardless of whether the purchase, production, or sale of merchandise is an income-producing factor.

> Benefits: The cash method of accounting ensures taxes are not paid on revenues that have not yet been received.

> Effective Date: Applies to taxable years beginning after December 31, 2017.
EXPANDED EXEMPTION FROM REQUIREMENT TO KEEP INVENTORY

Before TCJA: In order to clearly reflect income, a taxpayer had to account for inventories if the production, purchase, or sale of merchandise was an income-producing factor to the taxpayer. Furthermore, taxpayers that were required to account for inventories were also required to use the accrual method of accounting regarding purchases and sales. Two exceptions were provided: (1) taxpayers whose average annual gross receipts did not exceed $1 million, and (2) taxpayers in certain industries whose average annual gross receipts did not exceed $10 million, that treated inventory as non-incidental material and supplies.

After TCJA: Taxpayers with average annual gross receipts of $25 million or less are exempt from the requirement to account for inventories under Section 471 of the Code and have the option to use a method of accounting for inventories that either: (1) treats inventories as non-incidental materials and supplies, or (2) conforms to the taxpayer’s financial accounting treatment of inventories.

- **Benefits:** The taxpayer is not required to keep an inventory schedule if the $25 million gross receipts test is met.
- **Effective Date:** Applies to taxable years beginning after December 31, 2017.

EXPANDED EXEMPTION FROM UNIFORM CAPITALIZATION (UNICAP) REQUIREMENTS

Before TCJA: The uniform capitalization rules require certain direct and indirect costs allocable to real or tangible personal property produced by the taxpayer to either be included in inventory or capitalized in the basis of such property. Under Section 263A of the Code, resellers of real or personal property were required to include certain direct and indirect costs allocable to such property in inventory. A few exceptions are provided by Section 263A to the general UNICAP rules, such as the exception for resellers of personal property with average annual gross receipts of $10 million or less.

After TCJA: The exception for small taxpayers from the UNICAP rules was expanded under the TCJA. Under the new law, any producer or reseller that meets the $25 million gross receipts test is exempted from the application of section 263A, including the sale of self-constructed assets.

- **Benefits:** Producers and resellers that are now exempt from the Section 263A adjustment do not need to capitalize the allocable portion of overhead to inventory, allowing them to deduct these costs currently.
- **Effective Date:** Applies to taxable years beginning after December 31, 2017.

*Tax Shelters Defined*

The most commonly cited definition of a tax shelter in the Internal Revenue Code is (1) “a partnership or other entity, any investment plan or arrangement, or any other plan or arrangement if a significant purpose of such partnership, entity, plan, or arrangement is the avoidance of evasion of Federal income tax.” However, the IRC provides two additional definitions: (2) “Any enterprise (other than a C-corporation) if at any time interests in such enterprise have been offered for sale in any offering required to be registered with any federal or state agency having the authority to regulate the offering of securities for sale,” and (3) “Any syndicate.”
EXPANDED EXEMPTION FROM PERCENTAGE-OF-COMPLETION METHOD FOR LONG-TERM CONTRACTS

Before TCJA: An exception from the requirement to use the percentage-of-completion method for long-term contracts was provided for certain “small construction contracts.” In order for a contract to fall under this category, it had to be a contract for the construction or improvement of real property and both: (1) expected (at the time such contract is entered into) to be completed within two years of commencement of the contract, and (2) performed by a taxpayer whose average gross receipts for the prior three taxable years do not exceed $10 million.

After TCJA: The aforementioned exception was expanded under the new law in that the $10 million gross receipts threshold was increased to $25 million.

Benefits: By using the completed contract method rather than percentage-of-completion for long-term contracts, an opportunity exists to defer tax due until the job is complete. Under the completed contract method, costs are capitalized into the contract, but net profit is deferred until the contract is substantially complete.

Effective Date: The changes made to this provision are on a cut-off basis and therefore only apply to long-term construction contracts entered into after December 31, 2017, or taxable years ending after December 31, 2017.

TIMING OF REVENUE RECOGNITION

Before TCJA: An accrual basis taxpayer was required to recognize income when all the events that fix the right to receive such income had occurred and the amount thereof could be determined with reasonable accuracy, more commonly known as the “all events test.”

After TCJA: Under the new law, an accrual basis taxpayer subject to the all events test for an item of gross income is required to recognize income no later than the taxable year in which such income is taken into account as revenue in either an applicable financial statement or another statement that Treasury and the IRS identify as applying for this purpose. These new requirements do not apply to income items for which the taxpayer uses another “special method of accounting” provided in the Code, for example, percentage-of-completion for long-term contracts under section 460.

Consequences: The new provision may require recognition of gross income for tax purposes earlier than the previous law, which consequently may accelerate when income taxes are payable for certain businesses.

Effective Date: The “all events test” is deemed satisfied when the income is recognized on the financial statement for tax years beginning after December 31, 2017.

ACTION STEPS

On August 3, 2018, the IRS issued a Revenue Procedure 2018-40 which permits eligible small business taxpayers to obtain automatic consent from the IRS when a taxpayer wants to change to one or more of the new TCJA-permitted methods of accounting. Reach out to your local Marcum tax professional to learn more about the opportunities that may exist for businesses under the TCJA.
Pass-through entities have historically provided a more tax-efficient structure than C-corporations, but is this still the case? The Tax Cuts and Jobs Act (TCJA) of 2017 reduced the corporate tax rate to a flat 21% for tax years beginning after December 31, 2017. The TCJA also repealed the corporate Alternative Minimum Tax (AMT) and changed the requirements to qualify for the cash method of accounting, allowing taxpayers with average gross receipts of $25 million (indexed for inflation) or less for the prior three taxable years to now qualify. As a result, many taxpayers are reassessing their current entity structures to determine if they should switch from being a pass-through entity to become a C-corporation. This assessment requires careful analysis, as there are many factors that must be considered; some of these factors are not tax-related and are beyond the scope of this article.

The first, and perhaps the most attractive, factor is the difference in the marginal tax rates. Pass-through entities generally are not subject to federal income taxes. Instead, each owner of the entity pays the income tax liability on his or her allocable share of the pass-through income. Moreover, owners of pass-through entities operating in states that do not have an individual income tax should consider the state tax implications of converting the business to a C-corporation. For instance, the owners of a pass-through entity operating in Florida are not subject to state income tax. Conversely, a C-corporation is subject to a flat state tax of 5.5%. Considering that state income taxes are allowed as a deduction on the federal tax return, the C-corporation would be subject to a combined effective federal and state income tax rate of approximately 25.3%. As this example illustrates, a pass-through entity that qualifies for the QBI deduction may only reduce its effective tax rate by approximately 4.3 percentage points if it converts to C-corporation status -- not 16.

Another important factor in analyzing the impact of a C-corporation conversion is the taxation of distributions. Owners of pass-through entities are taxed on their allocable share of the business income, even if the cash is not distributed. Subsequent distributions of the income, however, can be made tax-free. Yet, there may be valid business reasons for keeping the earnings in the entity. One such reason could be to provide necessary working capital for the business. Another may be to provide for contingencies such as the payment of a potential lawsuit. In a pass-through entity scenario, the taxation of the income would be accelerated and would not coincide with the timing of the cash distributions to the owners. A C-corporation may be more advantageous in this case. Assuming that the pass-through entity did not qualify for the QBI deduction, the undistributed income would be taxed at a marginal federal tax rate of up to 37%. A C-corporation in the same situation, however, would only pay a flat tax of 21%.
Nonetheless, it is important to note that a C-corporation cannot avoid paying dividends without having a reasonable business need; otherwise, it risks becoming subject to a 20% tax known as the Accumulated Earnings Tax. The reasonableness of anticipated needs should be judged on the facts existing at the close of the year, and because the burden of proof rests with the taxpayer, it is crucial to have proper documentation.

Finally, although the TCJA significantly reduced the corporate tax rate, it did not eliminate double taxation. That is, earnings of a C-corporation are taxable to the entity at a federal rate of 21% and are also taxed to the shareholder when the dividend is paid, at a rate of up to 23.8%. Ignoring state taxes, that’s a total tax rate of 44.8%. If an owner of a profitable pass-through entity distributes the earnings every year, then the C-corporation structure may not be the most tax-efficient. Converting to a C-corporation may also be disadvantageous if the owner is contemplating an exit strategy in the near future. Assuming that the transaction were structured as an asset sale, the C-corporation would pay federal tax on the gain at a rate of 21%. The shareholder would also recognize a gain on the difference between the subsequent cash distribution and the adjusted basis of the stock. The tax rate on the gain can be as high as 23.8%.

**ACTION STEPS**

Whether a pass-through entity should convert to become a C-corporation, given the enactment of the TCJA, depends on each taxpayer’s unique circumstances. This is a consideration that requires careful analysis and planning. In the case of an S corporation, it is particularly important to consider the long-term effects of converting because once the S election is terminated, the entity cannot reelect S status for at least five years following the revocation. Failure to diligently consider all ramifications of a conversion may result in detrimental tax consequences down the road.

For assistance in evaluating the optimal structure for your business under the new rules of the TCJA and in planning your short- and long-term tax strategies, contact your Marcum tax professional.
The federal Research and Development (R&D) Tax Credit provides significant benefits to taxpayers with qualifying expenses. Recent changes in law in the Tax Cuts and Jobs Act (TCJA) and the 2015 Protecting Americans from Tax Hikes (PATH) Act have made the R&D credit even more lucrative, by providing taxpayers potentially larger credits for tax years ending after December 31, 2017. Changes in both of these laws make the R&D credit a very powerful tool to reduce a taxpayer’s tax liability and increase cash flow.

The R&D credit is a federal program and is available to businesses in most industries, including, but not limited to:

- Manufacturing
- Architecture & Engineering
- Software & Technology
- Financial and Professional Services
- Environmental & Life Sciences
- Construction

**PATH ACT CHANGES**
Changes to the PATH Act made the R&D Tax Credit permanent for tax years beginning after December 31, 2015. The Act also allows the R&D credit to be applied against the employer portion of OASDI (Social Security) of the payroll taxes for “qualified small businesses.” A qualified small business is defined as follows:

- A company with gross receipts of less than $5 million for the present tax year.
- A company that did not exist or have gross receipts in any tax year prior to the 5-tax-year period ending with the current tax year.
- A company that has qualifying research activities and expenditures.
- A company that has payroll tax liabilities.

The payroll credit is limited to $250,000 per year for up to five years, and any unused portion can be carried forward to future years.

The tax credit may also be claimed if the business uses a certified Professional Employer Organization (PEO). This provision allows qualified small businesses the ability to utilize the R&D credit against payroll taxes, where previously they might not have had the opportunity to utilize the credit due to the absence of taxable income.

**ALTERNATIVE MINIMUM TAX RELIEF**
Another benefit added as part of the PATH Act was the ability to utilize the R&D credit to offset Alternative Minimum Tax (AMT) for taxpayers with $50 million or less in average annual gross receipts, based on the three preceding tax years.
TAX CREDIT GUIDELINES

The R&D credit is calculated by determining the amount of Qualified Research Expenditures (QREs) for the company’s current and prior tax years. The QREs are made up of wages, supplies used in R&D development, and 65% of fees from third party contractors.

In order to meet the definition of qualified research expenditures, research activities performed in the United States need to satisfy a “Four-Part Test”:

1. The work is being performed to develop a new or improved business component (product, process, technique, formula, invention, or computer software component).

2. The activities are performed to discover information that is technological in nature. The activities involve physical, biological, engineering, or computer sciences.

3. The research is performed to eliminate technical uncertainty, determine if a desired result could be achieved, how to achieve it, or determine the specific design of a product.

4. The activities include a process of experimentation involving identification of the technical uncertainties, alternatives to consider in eliminating the uncertainties, and a process for evaluating alternatives.

ACTION STEPS

The TCJA and PATH Act have significantly increased the value of the R&D Tax Credit and the opportunity to consider its impact in year-end tax planning. In addition to the federal credit, many states have their own Research & Development credits, making this potential tax strategy even more beneficial. Effectively using the R&D credit will help increase a company’s cash flow by reducing taxes and the amount of quarterly estimates due. Companies may also be eligible to claim the credit for prior years.

Contact your Marcum professional to determine whether your company may qualify.
One unique provision of the Tax Cut and Jobs Act (TCJA) of 2017 is a new federal incentive called Qualified Opportunity Zones (“QOZ”). The goal of this new provision is to encourage capital investment in certain low-income communities within the United States. The IRS has approved census tracts for all 50 states and the District of Columbia that qualify for Opportunity Zone investments.

The new provision allows capital gains that are “reinvested” in a Qualified Opportunity Zone Fund (“QOZF”) to be temporarily deferred from being included in the investor’s gross income. A taxpayer may defer up to 100% of realized capital gain if the capital gain is reinvested into a Qualified Opportunity Fund within 180 days from the date of the sale of the asset.

If the investment in the QOF is held by the taxpayer for at least five years, the basis is increased by 10% of the original deferred gain. If the taxpayer holds the investment for at least seven years, the basis is increased by an additional 5%. The deferred gain is recognized on the date on which the QOF investment is liquidated or December 31, 2026, whichever comes first.

The provision also excludes from gross income the post-acquisition capital gain on investments in QOZF.s that are held for at least 10 years. For the sale of a QOZF investment held for more than 10 years, the taxpayer can make an election to convert the basis of such investment to the fair market value of the investment at the date of sale, thus creating no gain recognition. Taxpayers can continue to recognize losses associated with investments in QOZF.

A QOZF is an investment vehicle organized as a corporation or a partnership for the purpose of investing in a Qualified Opportunity Zone Property (“QOZP”) subject to certain requirements (below). QOZP includes any Qualified Opportunity Zone Stock (“QOZS”), Qualified Opportunity Zone Partnership Interest (“QOZPI”) or Qualified Opportunity Zone Business Property (“QOZBP”).
HOW DOES THE OPPORTUNITY ZONE WORK?
There are three ways to invest in an Opportunity Zone in order to defer and/or eliminate capital gains:

1. **Qualified Opportunity Zone Business** – If a trade or business meets certain requirements, including maintaining substantially all of the tangible property used by the trade or business within a Qualified Opportunity Zone (“QOZ”), it will be designated a Qualified Opportunity Zone Business (“QOZB”).

2. **Qualified Opportunity Zone Property** – If an investment in a QOZB is made by purchasing Qualified Opportunity Zone Stock (“QOZS”), a Qualified Opportunity Zone Partnership Interest (“QOZPI”), or the tangible assets in a Qualified Opportunity Zone Business Property (“QOZBP”), the investment will be considered a Qualified Opportunity Zone Property (“QOZP”).

3. **Qualified Opportunity Fund** - A fund that is set up as a corporation or a partnership and invests 90% of its assets in Qualified Opportunity Zone Property is a Qualified Opportunity Fund (“QOF”). The fund is subject to certain testing dates every six months to ensure 90% of its assets remain in the QOZ.

**ACTION STEPS**
For further information or to verify whether an address is located in an Opportunity Zone, contact your Marcum professional.

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**Taxpayer**

**Rollover $$ Within 180 Days**

1. If you have a trade or business that operates in a Qualified Opportunity Zone, that is generally a Qualified Opportunity Zone Business

2. Investing in that business’s stock, partnership units or assets directly is an investment in Qualified Opportunity Zone Business Property

3. A fund that invests 90% of its assets in Qualified Opportunity Zone Property is a Qualified Opportunity Fund
Top Ten Items Contractors Need to Know about the Tax Cuts and Jobs Act

THE NEW ACT PROVIDES FOR MANY POSITIVE CHANGES FOR CONTRACTORS.

The Tax Cuts and Jobs Act of 2017 is arguably the most significant piece of legislation passed during the Trump presidency to date and included the most substantial changes to the tax code in more than 30 years. The bill was touted as a simplification of the tax code that would offer both American businesses and individuals tax incentives and tax savings. However, both time and budgetary constraints necessitated that the bill be written, rewritten, and passed quickly. As a result, the final piece of legislation included many significant provisions that still need clarity, and out of necessity, includes a lot of “give and take” in terms of tax incentives offered. Following are the top 10 changes that will affect contractors in 2018 and beyond.
FLAT 21% TAX RATE FOR C-CORPORATIONS AND CHANGES TO CORPORATE NET OPERATING LOSSES

“The Give”: Lower Corporate Tax Rate
Effective in 2018, C-corporations will be subject to a flat 21% tax rate rather than four brackets ranging from 15% to 35%. (Fiscal year filers will utilize a prorated blended rate schedule based on year-end). For the construction industry, this generally translates to a tax cut for corporations with net income in excess of $120,000. The examples below help to illustrate the effect of the new rates:

<table>
<thead>
<tr>
<th>C-Corporation with 12/31 Year-End</th>
<th>2017</th>
<th>2018</th>
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</thead>
<tbody>
<tr>
<td>Net Income</td>
<td>$500,000</td>
<td>$500,000</td>
</tr>
<tr>
<td>9% DPAD Deduction (eliminated by tax act)</td>
<td>(45,000)</td>
<td>(45,000)</td>
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<tr>
<td>Taxable Income</td>
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<tr>
<td>Total Tax</td>
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<tr>
<td>Effective Tax Rate</td>
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</table>

<table>
<thead>
<tr>
<th>C-Corporation with 06/30 Year-End</th>
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</thead>
<tbody>
<tr>
<td>6/30/2017</td>
</tr>
<tr>
<td>Net Income</td>
</tr>
<tr>
<td>9% DPAD Deduction (eliminated by tax act)</td>
</tr>
<tr>
<td>Taxable Income</td>
</tr>
<tr>
<td>Tax under 2017 rates prorated for 184 days</td>
</tr>
<tr>
<td>Tax under 2018 rates prorated for 181 days</td>
</tr>
<tr>
<td>Total Tax</td>
</tr>
<tr>
<td>Effective Tax Rate</td>
</tr>
</tbody>
</table>

“The Take”: Net Operating Loss (NOL) Limitations
While there are no changes to a corporation’s NOLs generated prior to 2018, losses arising in tax years ending after December 31, 2017, will no longer be permitted to be carried back and will be available to be carried forward indefinitely. In addition, utilization of post-2017 generated NOLs will be limited to 80% of taxable income. In income years where NOLs are utilized, in 2018 or later taxable income will not be able to be reduced to zero by post-2017 losses.

Recommendation:
Business owners should analyze the potential savings of converting to a C-corporation compared to their current entity structure to determine which entity type is most beneficial.
For tax years ending after December 31, 2017, the Act eliminates the Domestic Production Activity Deduction, a popular deduction typically available to manufacturers, contractors, engineers, and architects.

**ADDITION OF THE 20% QUALIFIED BUSINESS INCOME (QBI) DEDUCTION AND ELIMINATION OF THE 9% DOMESTIC PRODUCTION ACTIVITIES DEDUCTION (DPAD)**

**“The Give”: 20% QBI Deduction**

Owners of pass-through businesses such as S-corporations, LLCs, partnerships, and sole proprietorships will be entitled to a deduction equal to 20% of the business income on their individual tax return. For single taxpayers with taxable income exceeding $157,500 ($315,000 Married filing joint), this 20% deduction can be limited for companies with minimal payroll expenses and capital expenditures. The deduction is limited to the greater of:

a) 50% of W-2 wages, or

b) 25% of W-2 wages plus 2.5% of the cost of qualified business assets.

Such limitations should not impact most construction contractors but may impact other commonly owned, ancillary businesses (real estate, for example). An election can be made at the individual taxpayer level to mitigate this potential problem and make more of the ancillary income qualify for the QBI deduction.

The chart below reflects a comparison of a married couple’s tax liability with pass-through net income of $500,000 and no itemized deductions, and the effect that QBI will have on their 2018 income taxes:

**“The Take”: 9% Domestic Production Activities Deduction (DPAD)**

For tax years ending after December 31, 2017, the Act eliminates the Domestic Production Activity Deduction, a popular deduction typically available to manufacturers, contractors, engineers, and architects.

Note: While the gap between the new corporate and individual tax rates may make a high-earning C-corporation appear desirable, many factors need to be considered before making such a decision. The double taxation of distributions from the corporation (i.e., dividends or property/cash distributions upon sale of the company’s assets) can quickly negate any lower front-end tax rate. Entities need to review all relevant facts and circumstances before deciding to form or convert to C-corporation status.

**Recommendation**

Individuals owning multiple businesses should determine the availability of making an election to aggregate if the QBI deductions will be limited.
EXPENSING 100% OF THE COST OF DEPRECIABLE ASSETS

“The Give”: Accelerated Depreciation

Equipment purchased after September 27, 2017, and before January 1, 2023, may be entirely expensed under new bonus depreciation rules. Prior law allowed for the deduction of 50% of the cost of new assets and was scheduled to phase out by 2020. The new tax law allows assets – either new or used – to qualify for the 100% deduction as long as it is the business’ first use of that asset.

The Section 179 deduction (which allows the write-off of purchased assets) has been increased from its current limit of $510,000 to $1,000,000. Assets purchased to improve nonresidential real estate, such as roofs, HVAC systems, and fire protection systems, now qualify for this special deduction. Previously, such improvements were required to be depreciated over a longer period. Between bonus depreciation and Section 179, most assets acquired by a construction company will be fully deducted in the year of acquisition.

“The Take”: Like Kind Exchanges and Qualified Improvement Property

A trade-off to the 100% depreciation is the elimination of “like-kind exchanges” on trade-ins of equipment. Previously, a business owner could trade in equipment when purchasing a similar piece and not recognize gain on the trade-in value. The tax law now limits that gain deferral only to real estate assets.

Note: Many states continue to disallow bonus and/or Section 179 depreciation.

Recommendation:

Businesses should carefully analyze their equipment needs to determine if additional property is a necessity, rather than spending funds to save taxes.

MORE CONTRACTORS CAN USE CASH OR COMPLETED CONTRACT METHOD TO REPORT INCOME

“The Give”: The Gross Receipts Limitation for use of cash method accounting has been increased to $25 Million

Contractors with average annual gross receipts of up to $25 million will be able to use the cash or completed contract method for tax purposes. Three prior years of revenue is averaged to determine the taxpayer’s average annual gross receipts for the purposes of this test. For some construction companies, this may be the most important change in the new law.

Since 1986 the tax code has used a revenue threshold of $10 million ($5 million for corporations and partnerships with corporate partners) as the definitive line between a “small” and “large” contractor. A large contractor is required to report gross profit from long-term projects under the percentage-of-completion method. As a result, the ability to defer recognition of income for tax purposes is diminished. Going forward, the $25 million limitation will be indexed for inflation on an annual basis.

Beginning in 2018, contractors that fall below the new revenue threshold will be exempt from reporting income on the percentage-of-completion basis. If the taxpayer previously exceeded the $10 million amount and filed returns utilizing a non-cash method, the business will be allowed to automatically change its method of accounting for long-term contracts to the cash or completed contract method for tax purposes. For the first three years beginning after December 31, 2017, the change will be automatic (by filing a Form 3115 and making the applicable 481(a) adjustment), even if an election was made in the prior five years. Contractors should review their business models to determine which method is most beneficial. Those operating under the $25 million limit should consider which method would be most advantageous going forward.

“The Take”: None, really. This change is very positive for contractors.

Recommendation:

Businesses should analyze their related parties to determine if, and how much, of the related party’s gross receipts need to be included when calculating average annual gross receipts. Also, businesses should analyze the effects of any accounting method change before making an election. Don’t assume the method currently used is worse.
ELIMINATION OF THE CORPORATE ALTERNATIVE MINIMUM TAX

“The Give”: No More Corporate AMT
The Alternative Minimum Tax (AMT) has been repealed for C-corporations but remains intact for individuals. Owners of companies were often subject to AMT as a result of accelerated depreciation of equipment, the treatment of long-term contracts, and a disallowance of state taxes.

Regarding C-corporations, small contractors using the completed contract method were previously required to recalculate alternative minimum taxable income (AMTI) using the percentage-of-completion method, resulting in large add-backs of the completed contract deferral. Going forward, with the elimination of the corporate AMT, this will no longer be the case. Large contractors that do residential construction will also benefit from the elimination of the AMT, as the 30% residential deferral will no longer need to be added back to calculate AMTI. C-corporations that previously paid AMT may also have outstanding AMT tax credits, which are now refundable.

Regarding individuals, exemption and phase-out amounts within the calculation have been raised, which should mean fewer taxpayers will pay the AMT. The adjustments for accelerated depreciation, the treatment of long-term contracts, and state taxes among other factors, will still need to be made.

“The Take”: Regular Tax More Closely Resembles AMT
On a corporate and individual level, the regular tax laws will more closely resemble those of the AMT, withlower rates, fewer allowable deductions, and limitations on loss utilization.

Recommendation:
Businesses should analyze prior returns to determine if there are any historical AMT tax credits. These credits do not expire and could have been improperly tracked through the years.

LOWER INDIVIDUAL TAX RATES AND DEDUCTION CHANGES

“The Give”: Lower Individual Tax Rates
Most taxpayers should see a lower effective tax rate due to shifts in individual tax brackets. The largest reduction occurs within the highest tax bracket. In 2017, income over $470,700 is taxed at the top marginal rate of 39.6%, while in 2018 the highest bracket begins at $600,000 and is 37%. See chart below.

“The Take”: Deductions are More Limited
About 30% of taxpayers currently itemize deductions, and the Tax Act was designed to reduce that number (simplification!). Highlights of the changes effective in 2018 include:

<table>
<thead>
<tr>
<th>Tax Rate</th>
<th>From</th>
<th>To</th>
<th>Total Tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>10%</td>
<td>$0</td>
<td>$19,050</td>
<td>$22,900</td>
</tr>
<tr>
<td>12%</td>
<td>$19,050</td>
<td>77,400</td>
<td>$96,450</td>
</tr>
<tr>
<td>22%</td>
<td>77,400</td>
<td>165,000</td>
<td>$92,600</td>
</tr>
<tr>
<td>24%</td>
<td>165,000</td>
<td>315,000</td>
<td>$150,000</td>
</tr>
<tr>
<td>32%</td>
<td>315,000</td>
<td>600,000</td>
<td>$285,000</td>
</tr>
<tr>
<td>35%</td>
<td>600,000</td>
<td>$∞</td>
<td>$∞</td>
</tr>
<tr>
<td>37%</td>
<td>$∞</td>
<td>$∞</td>
<td>$∞</td>
</tr>
</tbody>
</table>

a) The standard deduction has been almost doubled to $12,000 for single taxpayers and $24,000 for Married filing joint, and personal exemptions have been eliminated.

b) The deduction for state and local income, sales, and property taxes is capped at $10,000, adversely impacting taxpayers in states such as New York, New Jersey, Connecticut, and California.
c) Mortgage interest will be deductible for debt balances of $750,000 and less, whereas the limitation was $1 million previously, and interest on home equity loans is no longer deductible unless the funds are directly connected to the underlying property.

d) The phase-out of 3% itemized deductions for taxpayers with incomes in excess of $313,800 (Married filing joint in 2017) is eliminated by the new law in 2018 and beyond.

Aggregate business loss deductions are also limited to $500,000 for individuals. In the case of an individual who makes $1 million in wages and has $1 million in business losses, those losses are limited to $500,000 and the remaining $500,000 loss is carried forward. This is particularly important when planning owners’ compensation for loss companies.

**Recommendation:**
Individuals should determine if their state has developed a way to circumvent the limitation on state and local taxes.

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7

**LIMITATION ON INTEREST EXPENSE DEDUCTIONS**

*“The Give”: None*

*“The Take”: Deductibility of Business Interest Expense is Limited*

Starting in 2018, deductible interest expense will be limited to 30% of the business’s adjusted taxable income (see below). Businesses with gross receipts under $25 million will be exempt from this rule. Real estate entities may opt-out of this rule, but will sacrifice accelerated depreciation deductions. A large contractor with high levels of debt should be cognizant of this limitation and may find it beneficial to reduce or renegotiate debt to avoid triggering the limitation. (Interest expense in excess of the 30% threshold may be carried over indefinitely).

The following example reflects two companies with earnings before interest, taxes, depreciation, and amortization (EBITDA) of $2,000,000, which limits interest expense to a maximum of $600,000 (30%). $150,000 of Company B’s interest expense is therefore non-deductible in the current year (but can be carried forward indefinitely):

<table>
<thead>
<tr>
<th></th>
<th>Company A</th>
<th>Company B</th>
</tr>
</thead>
<tbody>
<tr>
<td>Revenue</td>
<td>$10,000,000</td>
<td>$10,000,000</td>
</tr>
<tr>
<td>Direct Costs</td>
<td>(9,000,000)</td>
<td>(9,000,000)</td>
</tr>
<tr>
<td>Gross profit</td>
<td>7,000,000</td>
<td>7,000,000</td>
</tr>
<tr>
<td>General and administrative expenses</td>
<td>(5,000,000)</td>
<td>(5,000,000)</td>
</tr>
<tr>
<td>Earnings Before Interest, Taxes, Depreciation, and Amortization (EBITDA) - “Adjusted Taxable Income”</td>
<td>2,000,000</td>
<td>2,000,000</td>
</tr>
<tr>
<td>Depreciation</td>
<td>(1,000,000)</td>
<td>(1,000,000)</td>
</tr>
<tr>
<td>Interest Expense</td>
<td>(500,000)</td>
<td>(750,000)</td>
</tr>
<tr>
<td>Non-deductible interest expense (&gt; than 30% of EBITDA)</td>
<td>-</td>
<td>150,000</td>
</tr>
<tr>
<td>Total Taxable Income</td>
<td>$500,000</td>
<td>$400,000</td>
</tr>
<tr>
<td>Interest expense limitation (30% of EBITDA)</td>
<td>600,000</td>
<td>600,000</td>
</tr>
</tbody>
</table>

*Note: This limitation is calculated at the entity level. Any limited interest is carried forward and must be tracked at the shareholder/member level.*

**Recommendation:**
Businesses should consider restructuring their debt, if possible, to lower interest payments if it is anticipated that interest expense may be limited.
**8  GIFT AND ESTATE TAX EXCLUSION DOUBLED**

"The Give": Huge Increases in Gift & Estate Tax Exclusions

Important to those performing succession and estate planning, the gift and estate tax exclusion amount has been doubled from $5.49 million to $11,180,000 per person, or $22,360,000 for married couples. This will allow a larger amount of assets, such as business interests, stock, and real estate, to be transferred to heirs tax-free. At the highest tax rate of nearly 40%, each additional million dollars of exclusion equates to up to $400,000 in tax savings.

"The Take": None

**Recommendation:**
High net worth individuals should consider making gifts to take advantage of increased exclusions, in case future legislation reduces this benefit.

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**9  ENTERTAINMENT EXPENSE DEDUCTION ELIMINATED**

"The Give": None

"The Take": More Conservative Rules Regarding the Deductibility of Meals & Entertainment

The two biggest impacts to the deductibility of meals and entertainment expense are the loss of the deduction for entertainment expense and the 50% limitation on meals provided to employees at the convenience of the employer. The deduction for business meals with clients remains at 50%, but any tickets for client entertainment can no longer be deducted. Meals provided to employees at the convenience of the employer were formerly 100% deductible and will now be limited to 50% deductibility. Expenses for events such as company parties, meals provided during training, and the like remain fully deductible.

**Recommendation:**
Businesses should be certain to record such expenses clearly and separately in their books to prevent the mingling of deductible and non-deductible costs.

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**10  PREVIOUSLY UNTAXED FOREIGN EARNINGS ARE NOW TAXABLE**

"The Give": Reduced Tax Rates

"The Take": Mandatory Inclusion of Foreign Earnings

Under prior law, if a U.S. shareholder were an owner of a controlled foreign corporation (CFC), the earnings of the CFC were not taxable in the United States until the money was distributed to the U.S. shareholder. Under the new law, all foreign accumulated earnings and profit are deemed to have been distributed on November 2, 2017, or December 31, 2017, whichever point is greater. To ease the tax burden, these amounts are taxed at either 8% or 15.5%, depending on the underlying assets of the CFC.

Going forward, a 10% shareholder of a controlled foreign corporation must include their share of "tested income," otherwise known as the Global Intangible Low-Taxed Income (GILTI). Benefits provided to C-corporations mitigate the effect of this inclusion and may potentially reduce any tax on this income inclusion to zero. In contrast, non-corporate shareholders are not entitled to these benefits, which may result in tax on this income of up to 37%.

**Recommendation:**
Businesses and individuals should review their foreign holdings to determine if they are subject to income inclusions. Non-corporate shareholders of controlled foreign corporations should consider setting up a U.S. corporate holding entity or converting the controlled foreign corporation to a foreign branch.

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**FINAL WORDS**

The new tax law brings with it a host of new challenges for contractors. A “technical corrections” bill usually follows major tax legislation to resolve unintended consequences. This will not be a good year for “business as usual!”
ONE OF THE MOST IMPACTFUL CHANGES MADE UNDER THE TAX CUTS AND JOBS ACT OF 2017 (ACT) PERTAINS TO ESTATE AND GIFT TAX LAW.

Under the Act, estate and gift taxes remain in place, but exemptions were raised to $11,180,000 for individuals and $22,360,000 for married couples. Those exemption levels expire in 2025, when they will revert to current levels (unless new law is enacted). Those levels are indexed again, but this time to the “chained” CPI index, which is lower. Calculations performed with this new index predict $6.3 million/$12.6 million exemptions in 2027. As part of the Act, the federal estate tax rate remains at 40 percent above the exemption. The gift tax stays at 40 percent.

The implications of all this are multifaceted and impact wealth and estate tax planning to varying degrees. We offer some key takeaways below as they pertain to personal wealth management, corporate and individual planning, life insurance planning and pension planning strategies.
GENERAL PLANNING TAKEAWAYS

- Heirs/designees of individuals who die in the next eight years will be subject to lower federal estate taxes.

- State estate taxes will still apply and remain at considerable levels in a number of states.

- Coupled with the $10,000 limitation on the federal deduction of real estate taxes and state income taxes, there may be a further physical migration to lower-tax states.

- The gifting exemption is also raised to the estate tax exemption limits cited above (i.e., $11,180,000 for individuals and $22,360,000 for married couples). This increased limit provides a planning opportunity for affluent individuals to make additional gifts to children and trusts. This is a “use it or lose it” provision; waiting until 2027 would allow the gifting amounts to revert to lower limits. There does not appear to be any “clawback” provisions in the new law.

- Gifting opportunities can also be coupled with existing techniques (e.g., discounting, GRATs, Intentionally Defective Trusts, CLATs) that were left untouched in the new tax law. These can provide even more leverage for gifting. Generation Skipping Trusts (GST) will be utilized more thoroughly in conjunction with the increased gifting limits.

CORPORATE AND INDIVIDUAL PLANNING TAKEAWAYS

- Eight-year Grantor-Retained Annuity Trusts (GRATs), designed to “roll out” before the new federal estate tax threshold expires, could be very effective in moving wealth to the next generation, with less risk of federal estate taxes in the event of a death during the GRAT term.

- There will be a swift return to “loan regime” split-dollar insurance programs for all corporations, since corporations will be more lightly taxed than previously and will benefit from substantially lower rates than individual tax rates. This provides a big planning opportunity for corporations via split-dollar, since the employer is “lending” money to the employee, and the low interest or economic benefit is the imputed cost.

- There will be a reduction in existing and newly implemented “executive bonus plans.” The deduction to the corporation is worth less, and the bonus will be taxed to the employee at a higher level than in the past. Many executive bonus plans will morph into split-dollar or deferred compensation plans.

- No longer will pass-through entities have to shy away from split-dollar plans; there is still tax leverage to be gained. Trusts can also leverage the new pass-through taxation rules.
LIFE INSURANCE PLANNING TAKEAWAYS

Life insurance will play a larger role in individuals’ overall financial portfolio due to tax savings, asset protection, income withdrawal ability, and reduced Alternative Minimum Tax (AMT) exposure. Life insurance as an “asset” class will be a more common term utilized by financial advisors.

Additionally, acquiring life insurance within a corporate structure will exhibit new advantages, while still maintaining the existing ones. Specifically:

- Accumulating monies within the insurance policy cash value will be even more tax advantageous.
- With corporations no longer subject to AMT, the extra tax drag on death benefits applicable to corporate-owned policies will disappear. Think key person, deferred comp, buy/sell coverage, all corporate-owned policies, etc.
- Deferred compensation in nonqualified plans will experience a resurgence. In the original House and Senate tax reform drafts, nonqualified deferred compensations would have been eliminated. Even existing plans would have gone away. Heavy lobbying occurred for that provision to be removed from the bills.

The bottom line is that life insurance expense will be less costly under the lower corporate brackets.

PENSION PLANNING TAKEAWAYS

- It’s likely that more Roth IRA conversions will occur, due to lower individual rates.
- If charitable contributions are discovered to have an “elastic” economic demand component correlated with the value of tax deductions, you may see a trend towards lower charitable contributions.
- Employees with the flexibility to change to a 1099 status may incorporate to take advantage of the new tax brackets and pension opportunities. However, they may be putting their healthcare and qualified benefits at risk by doing so and would have to acquire their own.

ACTION STEPS

All takeaways in this article represent educated opinions, and we certainly welcome any comments you wish to share. We will continue to closely monitor the landscape and keep you updated as developments occur. In light of the Act and its many ramifications, all life insurance policies, corporate and individual, should be reviewed along with their corresponding agreements and trusts.
The Tax Cuts and Jobs Act (TCJA) of 2017 introduced a wide array of changes to most areas of the tax law beginning with the 2018 tax year, including gift and estate taxes.

**ANNUAL EXCLUSION**
The 2018 annual gift exclusion is $15,000, increased from $14,000 in 2017. This exclusion is the amount you can give away per person per year tax-free. In addition, married couples can elect to split gifts. Utilizing this strategy, married taxpayers can gift up to $30,000 to an individual in 2018 before a gift tax return is required. Annual gifting is an excellent way to reduce the value of a taxpayer’s gross estate over time, thereby lowering the amount subject to estate tax upon date of death.

**LIFETIME EXEMPTION**
The 2018 lifetime gift exemption is $11,180,000 (indexed for inflation), which increased significantly from $5,490,000 in 2017. This exemption is the total amount you can give away over the course of your entire lifetime tax-free. The Act more than doubles the lifetime exemption, but only temporarily. It is scheduled to sunset at the end of 2025 unless Congress renews the provision, and the prior exemption amount will be restored, as indexed for inflation.

**PORTABILITY ELECTION**
The portability election remains under the Act. It is an imperative planning tool for taxpayers, especially if the death of a spouse occurs while the increased exemptions are in place. Portability allows the second spouse to have the benefit of the deceased spouse’s $11.18 million exemption, even if the second spouse dies when a lower exemption amount is in effect. Keep in mind that an estate tax return will need to be filed when the first spouse dies in order to make the portability election, even if the gross estate is under the filing threshold.
BASIS STEP-UP
No changes were made under TCJA to these provisions, which allow a step-up in tax basis for most inherited appreciated assets (excluding retirement accounts and annuities). Generally, basis is the amount paid for an asset. Upon death, the beneficiaries are allowed to increase the tax basis of an inherited asset to the fair market value at the date of the decedent’s death.

ESTATE PLANNING CONSIDERATION
Although you have until December 31, 2025, to take advantage of the increased gift tax exemption, making gifts sooner rather than later will allow you to remove future appreciation of gifted assets from your estate. You must, however, carefully weigh the loss of a step-up in income tax basis for any gifted asset when compared to the step-up in basis that would result if assets are held until death and included in your estate. This is especially relevant for those who do not anticipate having estates that exceed the exemption amount of $11.18 million for single people and $22.36 million for married couples.

Married people with estates below the threshold amount should focus on the following tax and non-tax considerations:
1) Whether assets should be bequeathed outright or in trust for a surviving spouse.
2) Maximizing step-up in basis on the surviving spouse’s death.
3) Taking advantage of portability.

SECTION 199A AND TRUSTS
The TCJA created a new Section 199A deduction, which allows certain taxpayers a 20% deduction on qualified business income (QBI). The 199A deduction has taxable income limitations, based on the taxpayer’s total income. In order to maximize the 199A deduction, taxpayers should consider utilizing non-grantor trusts, which are separate taxpayers, each eligible for the 199A deduction. (The proposed regulations under Section 199A prevent a taxpayer from establishing multiple trusts with the same grantor and beneficiaries for the principal purpose of avoiding income tax).

UPDATE ON INTERGENERATIONAL SPLIT DOLLAR
Intergenerational Split Dollar is a strategy used to minimize gift and estate taxes and involves large insurance premium payments. Under this technique, an adult child will purchase life insurance on his/her life (through a life insurance trust) and pay the premiums with a loan from the parent. Since the loan will not be paid back until the death of the child, that loan receivable is discounted in the parent’s estate (which results in an estate tax benefit to the parent).

In a settlement in the Cahill case in August 2018, the estate conceded to the IRS’s valuation of the note receivable of $9.6 million, instead of the estate’s reported value of $183,700. Due to the IRS victory in this case and other similar cases, you should not pursue this type of split-dollar arrangement if a discount on the receivable is a significant part of the plan.

ACTION STEPS
Now is a good time to meet with your Marcum tax professional to consider the best ways to make additional gifts using the increased exemption, as there are benefits to making the gifts now as opposed to waiting until the exemption is about to expire.
One of the most significant changes to the tax code under the Tax Cuts and Jobs Act (TCJA) of 2017 regards the deductibility of expenses for taxpayers who itemize deductions on their Form 1040. For many modern families, changes to the deductibility of medical expenses, including Assistive Reproductive Technology (ART), may be particularly problematic.

Generally, to the extent that medical expenses including ART exceed a certain percentage of Adjusted Gross Income (AGI), they can be deducted in the same year that expenses not reimbursed by healthcare insurance are paid. (For purposes of this discussion, AGI is basically all of an individual’s income prior to deductions or other decreases).

In 2017 and 2018, in order to be deductible, otherwise qualifying medical expenses must exceed 7.5% of AGI. Going forward for 2019 through 2025, qualifying medical expenses are only deductible to the extent they exceed 10% of AGI.

ART includes standard medical practices such as hormone therapy and sperm donation, more advanced procedures like IVF, as well as options where state law is still developing, such as the use of egg donation and surrogates.

Under the TCJA, all forms of ART are generally deductible, except the cost of surrogacy. Surrogacy is excluded because the expenses incurred in utilizing a surrogate are not expenses for medical procedures performed on the bodies of the taxpayer or the taxpayer’s spouse. Surrogacy requires the participation of a third party.
Herein lies the problematic issue for modern families. Opposite-sex couples, same-sex female couples, and single women can avail themselves of most types of ART and then deduct a significant portion of the expenses. However, for same-sex male couples and single men, the use of ART to produce a child requires, at a minimum, the use of both a surrogate and an egg donor. In addition to surrogacy and egg donation being two of the more expensive ART methodologies, when utilized by male couples or single men, none of these expenses are deductible. This is because neither egg donation nor surrogacy are procedures that affect the man’s body. The practical outcome is that some types of families are not able to utilize the tax law to defray the cost of conceiving, while other types of families are.

In September 2017, three months before the TCJA was passed, the 11th Circuit Court of Appeals decided *Morrissey v. U.S.*, which addressed the issue of deductibility of ART expenses incurred by a single man using IVF, egg donation, and surrogacy to conceive a child. The Court held that the expenses were not deductible as medical expenses because they were not incurred to perform medical procedures on the taxpayer, his spouse, or his dependents. In addition, the Court also found that the IRS application of the medical expense deduction rules, which produced an inequitable result when viewed broadly, did not violate the equal protection clause of the Fifth Amendment when viewed narrowly under Constitutional analysis.

For more than a half-century, Congress, the IRS, legal scholars, and the public have gone back and forth over the issue of medical expense deductions, especially expenses paid for ART medical services. *Morrissey* shows us that many modern family issues are still unresolved in the tax code, as elsewhere.

Beginning in 2019, the fundamental change to the tax code under TCJA will result in far fewer individuals itemizing their deductions. For those who do itemize, less of their annual medical costs will be deductible. In addition, the issues surrounding ART will continue to be debated, change will continue to be the norm, and these changes will continue to create special problems for modern families.

**ACTION STEPS**

In addition to causing the types of problems present in *Morrissey* and innumerable other cases, change also creates planning opportunities. As *Morrissey* shows, the tax code can sometimes work differently for modern families, and with the changes to the underlying tax law, this effect will likely be exacerbated. Marcum’s Modern Family & LGBT Services group remains on the cutting edge of issues facing modern families. Taxpayers will benefit by being ready for the changes that will affect them in 2019 and beyond. Speaking to your Marcum tax advisor to plan for the coming changes is a great first step.

"Beginning in 2019, the fundamental change to the tax code under TCJA will result in far fewer individuals itemizing their deductions."
State and Local Tax Updates

A SUMMARY OF RECENT SIGNIFICANT COURT CASES AND AN ANNUAL UPDATE OF STATE LAW CHANGES.

SALES TAX ECONOMIC NEXUS
On June 21, 2018, the United States Supreme Court in a 5-4 decision, ruled in favor of South Dakota and its economic nexus provisions for sales tax collection. In doing so, the Court overturned its prior decision in Quill (Quill Corp. v. North Dakota). Quill required that a retailer have a physical presence in a state in order to be required to collect sales tax for sales into that state. The statute upheld by the Court in South Dakota v. Wayfair, Inc. requires remote retailers with annual in-state sales exceeding $100,000, or 200 separate transactions, to collect and remit sales tax.

Since the decision, other states have started to implement sales tax economic nexus rules. Some of these rules went into effect as early as July 2018, with many more starting in October 2018 and January 2019. It is to be expected that most states will have some sales tax economic nexus rule. The majority of these rules will follow the South Dakota rules, but as is normal with state taxes, there will be many different augmentations.

Taxpayers have taken steps to keep up with the ever-changing rules in each state, making sure to register at the start date of the economic nexus laws as enforcement begins. It is not uncommon for clients that had previously had to file sales tax in only a few states are now filing in more than 20 states. Taxpayers have also been forced to understand the taxability of their products in these additional states, and depending on the industry involved and the tax jurisdiction, this can mean different answers.

Taxpayers that have not evaluated the implications of the new economic nexus rules are potentially liable for noncompliance. While sales tax is a tax on the consumer, the failure to collect the tax by a retailer that has nexus in the state is a liability to that retailer. The failure to properly collect sales tax isn’t just a business risk; it’s a common issue that surfaces in financial statement audits and due diligence analysis. The new sales tax laws are likely to bring an already common exposure item even more to the forefront.

FULFILLMENT BY AMAZON (FBA)
While the Wayfair decision helped to bring attention to sales tax, selling though Amazon remains a potential exposure item for both sales tax and income tax, which has been receiving more and more attention from state tax departments.

Fulfillment by Amazon (FBA) is a common sales channel for retailers online. Under this arrangement, companies send their inventories to Amazon, and then Amazon distributes the inventory across all of its warehouses. Sellers can access the location of their inventory via their Amazon portals. Since the retailer still owns the inventory, this creates nexus for the company in all of the states where Amazon holds it.

Generally, inventory is spread across substantially all of the warehouses in order to fulfill Amazon Prime shipping requirements. The nexus created by this arrangement applies to, but is not limited to sales tax, income tax, franchise tax, and gross receipts taxes.

Taxpayers who utilize Amazon FBA are commonly confused by the way state taxes accrue in their accounts. Amazon, by default, will collect and remit sales and use tax in a certain states including Pennsylvania, Oklahoma, and Washington, due to the special marketplace facilitator rules in those states. However, in the majority of states, Amazon will not automatically collect, and does not remit, sales tax.

The taxpayer’s inventory, which is likely dispersed to warehouses in more than 20 states, creates filing requirements which, in many cases, the taxpayer is not aware of. The non-collection of sales tax and the non-filing of income tax returns is something that the departments of revenue have started to audit. States such as California and Massachusetts have started to audit and assess tax against Amazon FBA sellers who have not been properly remitting taxes.

At the end of 2017, the Multistate Tax Commission offered a favorable voluntary disclosure agreement program in a select number of states; however, a follow up program is not certain to occur. Taxpayers with historical exposure can still file a voluntary disclosure agreement under the normal terms offered by states, in order to become compliant with their taxes and in most cases avoid penalties. In future periods, the taxpayers can take advantage of restructuring to mitigate the tax exposure created by selling through Amazon FBA.

Taxpayers who choose to do nothing are risking an audit on an issue that isn’t going to go away. The states have been receiving information related to Amazon FBA sellers, and since there is no statute of limitation for non-filers, audits can happen at any time in the future.
STATE-SPECIFIC UPDATES

Connecticut – On May 31, 2018, Senate Bill 11 was signed, creating a new pass-through entity tax in Connecticut. Instead of withholding income from the pass-through entity, a tax is now paid at the entity level, and a credit for the tax is allowed for the personal or corporate owner’s tax level. This new tax structure was created as a way to circumvent the $10,000 federal limit for individual state and local tax deductions.

California – In March 2018, the California Superior Court in San Francisco ruled in favor of the taxpayer in Paula Trust v. California Franchise Tax Board (FTB). The FTB has long taken the position that trusts are subject to tax on:
- All California-source income, plus
- Non-California-source income apportioned pro-rata, according to the number of California fiduciaries and non-contingent beneficiaries.

The Superior Court found for the first part of this approach, contrary to the law, relegating all trust income subject to apportionment. As a result of the decision, a trust with at least some nonresident fiduciaries or nonresident non-contingent beneficiaries may be able to defer California tax on California-source income earned by the trust until the income is distributed to beneficiaries.

Florida – On March 23, 2018, House Bill 7087 reduced the state tax rate on commercial rentals to 5.7%, effective January 1, 2019. Florida had previously decreased the rate from 6% to 5.8%, as of January 1, 2018. Other changes in the bill included updating Internal Revenue Code (IRC) conformity, sales tax exemption for nursing homes, two sales tax holidays, and property tax relief related to tropical storm damage.

Illinois – Effective January 1, 2018, the Illinois Revised Uniform Unclaimed Property Act made several significant changes to the existing law. Notable revisions include the following:
- The dormancy period (period of presumed abandonment) was reduced from 5 to 3 years, for most types of property;
- The business-to-business exemption for certain transactions between two business entities (accounts receivable, outstanding checks, etc.) was repealed; and
- The statute of limitation was extended from 5 years to 10 years.

Indiana – On March 23, 2018, SB 257 was signed, which temporarily exempts Software as a Service, or SaaS, from Indiana sales and use tax, effective July 1, 2018. Without future action, this provision will expire July 1, 2024. Previously, the state interpretations of the statutes and regulations by the department had concluded that SaaS was subject to the tax because of the taxability of prewritten computer software.

New Jersey – On July 1, 2018, Assembly Bill 4202/Senate Bill 2746 made significant changes to the corporation business tax. This law changes the net operating loss rules, increases the tax rate to 11.5%, and adopts market-based sourcing and mandatory combined reporting, along with other TCJA-related changes.
How the Tax Cuts and Jobs Act Affects State Taxation

HEADACHE OR WINDFALL FOR STATES?

The TCJA has created both headaches and windfalls for states, related to two primary issues. First, the limit on the federal deduction for state and local income tax along with real estate taxes, capped at $10,000 each year, has created pressure for some high-tax states such as NY, CT, CA, and NJ to look at ways to circumvent the limitation. These tax schemes are a direct result of pressure from state residents to find a way to reduce state taxes if the federal exemption is lost. Since the states will not seek to cut state taxes, the next best strategy is to convert the state income tax into an item that is deductible at the federal level. This concept has taken on two primary plans that have varying degrees of benefit to state residents.

The first revolves around states setting up state-run charitable entities to which residents can make voluntary contributions. The benefit for the resident is that the contribution will provide a credit that the resident can use to offset state income tax. Recommendations have also been made for local cities and towns to do the same in relation to real estate taxes.

The proposed program would work as follows: The state taxpayer would contribute $10,000 in cash to such a charity and, as a result, receive a tax credit of $10,000 to offset state income taxes. The contribution would be deductible at the federal level as a charitable contribution;

Unfortunately, the IRS has negated the benefit of this strategy by requiring the benefit received by the resident to offset the contribution. So in the example above, the resident would receive no contribution benefit, since 100% of the contribution would be returned as a tax credit. The only way to get a federal deduction would be for the tax credit to be limited to $5,000, at which point the contribution would then be $5,000. It is unlikely that anyone would seek to apply this strategy since the $10,000 state tax cost has now risen to $15,000 albeit, with a $5,000 federal charitable deduction.

The second issue created by the states is a method to convert state income taxes into corporate deductions via a new payroll tax in New York and a tax on pass-through entities in Connecticut. The IRS response to these strategies is somewhat unknown, but will be addressed fairly quickly in 2019 since, while New York has held off on its payroll tax until January 1, 2019, CT implemented its pass-through entity tax for 2018, so its application will affect 2018 tax returns.

The Connecticut Pass-Through Entity Tax is a 6.99% tax on the income of partnerships or S-corporations that are taxable in CT. There are two methods to calculate the tax: the standard method and the alternative method. For simplicity, we’ll only discuss the standard method, which is the default unless an election is made to use the alternative method.

Example 1: PE has $1,000 of ordinary income and has no other income. PE conducts business both within and without Connecticut and determines, based on facts not stated in this example, that its apportionment fraction is 10%. In this situation, PE has $100 of Connecticut source income ($1,000 * 10%) and a PE Tax liability of $6.99 ($100 * 6.99%).

Example 2: PE has $500 of Connecticut source income, including a distributive share of $200 of Connecticut source income that it received from Sub PE. PE is a partner in Sub PE. Sub PE filed a PE Tax Return and paid the PE Tax due. PE is subject to tax on $300 ($500-$200) of its Connecticut source income and has a PE Tax liability of $20.97 ($300 * 6.99%).

The partner in the entity is then entitled to a PE tax credit equal to 93.01% of the partner’s share of the PE tax liability. A partner’s share of the PE tax liability is determined based on the percentage of the partner’s distributive share of income that is included in the PE’s income, subject to the PE tax. Since the 6.99% PE tax is the highest personal income tax rate in CT, it is likely that the resident and non-resident partners will receive a credit in excess of their CT tax. The excess credit is treated as an overpayment and can be refunded to the partner. This strategy, thereby, converts the distributive share of income from a pass-through entity into a tax deduction on the entity which in turn reduces federal taxable income of the PE by the CT income tax that would be paid by the CT partners or shareholders. The IRS has not provided any comment on how it will view this tax strategy, but with returns due in March of 2019, taxpayers should expect some guidance by the end of 2018.
This issue in Connecticut helps owners of pass-through entities, but does nothing for those earning wages, which is being addressed by the New York Employer Compensation Expense Tax (ECET). This is a tax on the employer for wages paid to employees earning in excess of $40,000 annually beginning in 2019. The tax is being phased-in over three years as follows:

1. 1.5% in 2019.
2. 3% in 2020.
3. 5% in 2021 and subsequent years.

Employers that wish to participate in the ECET must make an annual affirmative election by December 1 to pay the optional tax in the following calendar year. Thus, the initial annual employer election must be made by December 1, 2018, for employers wishing to participate in the program in 2019. The New York State Department of Taxation and Finance will be providing a web-based registration system to facilitate the employer election into the ECET.

Once the election is made, employers will be required to pay the ECET electronically on the same dates as the employer’s withholding tax payments are required to be made. Filing dates for the quarterly ECET returns will also mirror the due dates of the employer’s withholding tax returns.

Employers are prohibited from deducting or withholding any portion of the tax from the employee's wages. Covered employees making over $40,000 will receive a credit when filing their personal income tax return and should review their 2019 Form IT-2104, Employee's Withholding Allowance Certificate, which will be updated to allow employees with wages subject to the tax to adjust their income tax withholding accordingly.

It should be noted that the IRS has not yet confirmed whether employers will be able to offset their federal income tax liability by taking a deduction based on payroll taxes paid to New York State under the framework of the ECET. Until the IRS provides further clarification as to the validity of employer deductions based on the ECET, employer incentives to participate in the program will remain unclear.

While this program appears beneficial, it is entirely voluntary by the employer, and since they cannot reduce employees’ wages by the tax, it is unlikely that many employers will make the election. The only way that it appears to be a workable solution for employers is if employees forgo annual raises in favor of the employer electing to pay the ECET. Were that to happen, it is not clear how the IRS would view this system, as the employee is obtaining a benefit in the form of a tax credit, and the IRS could determine that to be income, thus defeating the benefit to the employee.

Other states have espoused plans to implement similar strategies and are looking at the reaction of the IRS to these two plans. It is likely that whatever issue the IRS may take with either the CT or NY plans will then be adapted by the next state, until completely workable plans are implemented. The other issue out there is that the attorney generals of CT, NJ, NY, and MD have stated their intentions to sue the IRS, should it seek to impose restrictions on these workaround statutes. So, the issue bears watching to see who will blink first: the IRS or state government. Unfortunately, individual taxpayers are the ones in a state of limbo while state and federal governments rattle their sabers.
What's New for Tax Exempt Organizations

HOW THE NONPROFIT WORLD FARED WITH THE TAX CUTS AND JOBS ACT OF 2017

The Tax Cut and Jobs Act (TCJA) will impact almost every type of business organization. The following is a summary of provisions that nonprofit entities should be aware of:

UNRELATED BUSINESS TAXABLE INCOME (UBTI)
Beginning January 1, 2018, organizations carrying on more than one unrelated business activity must now separately calculate UBTI for each activity, a term referred to as “siloing.” As a result, losses from one trade or business may not be used to offset income derived from another trade or business. In enacting the legislation, Congress did not provide the exact criteria for determining how this is to be applied. Lingering open questions remain, such as:

- How does the nonprofit determine if a particular activity is a separate unrelated trade or business?
- Should investment holdings in multiple partnerships be considered one unrelated trade or business, or should they be treated separately?
- How should expenses for multiple unrelated trades or businesses be allocated?

On August 21, 2018, the Internal Revenue Service released Notice 2018-67 which provides temporary guidance on some of these points.

IS IT A SEPARATE TRADE OR BUSINESS?
The Notice provides that exempt organizations may rely on a reasonable, good-faith interpretation of Internal Revenue Code Sections 511 through 514, until final regulations are issued, when determining whether an exempt organization has more than one unrelated trade or business. Specifically, the proposed regulations state that “reasonable, good-faith interpretation” includes using the North American Industry Classification System (NAICS) 6-digit codes. The NAICS is a classification system for collecting, analyzing, and publishing statistical data related to the U.S. business economy. Exempt organizations that file Form 990-T to report UBTI are already using this code system when describing the organization’s unrelated trade or business.

SILOING RULES
The Notice also provides interim and transition rules for aggregating income from partnerships and debt-financed income from partnerships. An exempt organization may aggregate its UBTI from its interest in a single partnership with multiple trades or businesses conducted directly or through lower tier partnerships (“Qualifying Partnership Interest”) if one of two tests is met:

- A de minimis test, which the exempt organization satisfies if it holds directly no more than 2% of the capital and profits of the partnership; or
- A control test, which the exempt organization satisfies if it directly holds no more than 20% of the capital interest and lacks “control or influence” over the partnership.

In addition, a tax-exempt organization that acquired a partnership interest prior to August 21, 2018, may treat each partnership interest as a single trade or business, regardless of whether it meets either test or there is more than one trade or business directly or indirectly conducted by the partnership (or lower-tier partnerships).

ACTION STEPS
Tax-exempt organizations will benefit from reviewing their existing investment partnerships to determine (a) whether the interests satisfy either the de minimis or control tests and, (b) if it does not meet either test, what impact siloing each individual investment may have on the organization’s overall UBTI.
UNRELATED DEBT-FINANCED INCOME

The income from qualifying partnership interests permitted to be aggregated under the interim rule includes any unrelated debt-financed income that arises in connection with the qualifying partnership interest that meets the requirements of either the de minimis test or the control test (noted above).

The Notice provides an example illustrating the application of this interim rule:

A tax exempt organization has an interest in a hedge fund that is treated as a partnership for federal income tax purposes, the interest is a “qualifying partnership interest” that meets the requirements of the de minimis test, and the hedge fund regularly trades stock on margin. Ordinarily, the dividends from such stock and any income (or loss) from the sale, exchange, or other disposition of such stock would be excluded from UBTI. However, because all or a portion of the stock’s purchase is debt-financed, the exempt organization would be required to include all or a portion (depending on the debt-basis percentage applied) of the dividend income and any income (or loss) from the sale of the stock in UBTI. For the purpose of the interim rule, the exempt organization may aggregate unrelated debt-financed income generated by the hedge fund with any other UBTI generated by any of the hedge fund’s trades or businesses that are unrelated trades or businesses with respect to the exempt organization.

Similarly, any unrelated debt-financed income that arises in connection with one partnership interest may be aggregated with UBTI that arises in connection with other partnership interests.

While the IRS suggests that it “may be appropriate” to aggregate partnership interests in this manner, it is also requesting commentary regarding the treatment.

NET OPERATING LOSSES (NOL)

Prior to the Tax Cut and Job Act, an NOL could be carried back up to two tax years and forward up to 20 tax years to offset taxable income. The Tax Cut and Job Act made extensive changes to net operating losses including limiting post-2017 NOLs to the lesser of (1) the aggregate NOL carryovers to such year, plus the NOL carrybacks to such year, or (2) 80% of taxable income computed without regard to the deduction generally allowable. The changes to the NOL provisions would also affect tax exempt organizations with unrelated trade or business income and, in particular, such organizations with both pre-2018 and post-2017 NOLs.

UNRELATED BUSINESS INCOME TAX ON FRINGE BENEFITS TO EMPLOYEES

The Tax Cuts and Jobs Act of 2017 enacted a provision whereby tax exempt organizations that provide their employees with qualified transportation fringe benefits that are not included in their employees’ taxable income (i.e., parking reimbursements, mass transit passes, on-premises athletics facilities, etc.) must now include the value of such benefits as UBTI subject to unrelated business income tax. In other words, an expense is yielding unrelated business income tax.

In further guidance, Notice 2018-67 provides that UBTI arising from tax-exempt organizations’ parking and transportation benefits is not subject to the “silo” rule. Effectively, the tax exempt organizations, engaged in more than one unrelated trade or business, would be allowed to net their parking and transportation expenses against any other UBTI. This does not help many charities, churches, or other Section 501(c)(3) groups that are subject to unrelated business income tax for the first time under the new law, but it does provide some relief for organizations with multiple unrelated business income activities. The Notice does not provide any guidance with regard to computing the unrelated revenue.

To avoid the UBTI liability, an employer organization can consider providing such benefits as taxable income to the employees, discontinue providing the benefits, or increase pay to its employees.

NEW EXCISE TAX FOR LARGE UNIVERSITY ENDOWMENTS

An excise tax of 1.4% will be imposed on the net investment income of some private college and university endowments, where there is an enrollment of more than 500 students and an asset threshold of at least $500,000 per full-time student. The new law also makes a slight modification to the definition of “applicable educational institution,” which now includes only institutions with more than 50% of tuition-paying students located in the United States.
NEW EXCISE TAX ON HIGH SALARIES
An excise tax of 21% will be imposed on wages in excess of $1 million for any covered employee of a nonprofit entity. This tax, paid by the organization, is applicable to compensation in excess of $1 million for employees of a tax exempt organization who are one of the five highest-paid employees for the taxable year. A special exclusion applies to compensation paid to licensed medical professionals.

The excise tax applies to any “excess parachute payments,” which is compensation contingent upon termination of employment where the aggregate present value of the payments exceeds three times the employee’s average annual compensation.

This change is intended to bring nonprofit salary taxation into line with tax policies regulating for-profit corporations.

PHILANTHROPIC ENTERPRISE ACT OF 2017
The Philanthropic Enterprise Act was signed into law on February 9, 2018, largely impacting the private foundation sector by changing the excess business holding rules which generally prohibit a private foundation from owning more than 20% of a for-profit company, by imposing significant penalties for ownership exceeding this threshold. The bill was championed by Newman’s Own Foundation, which owns a 100 percent of No Limit, LLC, the for-profit that produces and sells the Newman’s Own brand of food products. The new law now allows a foundation to own 100 percent of a company if operated independently and all of its profits go to charity.

The new law effective, December 31, 2017, opens many opportunities for founders of companies that want to devote all profits from their businesses to charity by allowing them to place their companies under the ownership of a private foundation.

OTHER KEY OBSERVATIONS AND POTENTIAL ACTION STEPS:
Other TCJA changes that impact individuals will also have a direct impact on charities. For example, the individual adjusted gross income limitation was increased to 60%, from 50%, for cash contributions made to public charities by individuals. Tax exempt organizations should promote this benefit with donors to increase funding.

Complete guidance is still lacking in many areas of this new law; therefore, tax exempt organizations must carefully evaluate and strategically implement the best options to prevent any threat to their tax exempt status or cause unintended penalty consequences. To learn more about upcoming guidance and for advice on the impact of the Tax Cuts and Jobs Act of 2017 to your organization, contact your not-for-profit specialist at Marcum.
Qualified Transportation Fringe Benefits

THE NEW LAW IMPOSES BIG CHANGES TO EMPLOYERS’ QUALIFIED TRANSPORTATION BENEFITS.

One of the biggest unexpected surprises in the new tax law is the requirement that both for-profit and tax exempt organizations will no longer be allowed to expense transportation fringe benefits. In fact, tax-exempt entities are now required to report as unrelated business income (UBI) amounts paid or incurred for qualified transportation fringe benefits. These expenses include parking costs, as well as expenses related to traveling to and from work on subways, buses, or other similar commuter transit systems. (This rule, pertaining to tax exempt entities, was included in the tax law to maintain parity with for-profit organizations that are no longer able to deduct such expenses).

In March 2018, the IRS issued Publication 15-B, “Employer’s Tax Guide to Fringe Benefits.” Many tax professionals thought the law couldn’t possibly apply to employee deferrals of wages, reasoning that these were the employees’ own wages and that there was no benefit deduction to be disallowed. The new guide specifically states that qualified transportation fringe benefits include all such benefits regardless of who is paying! This will mean that for-profit companies will only be entitled to an expense if the employee includes the fringe in W-2 income.

The guide confirmed the non-deductibility of qualified transportation benefits, whether provided directly by the company, through a bona fide reimbursement arrangement, or through a compensation reduction agreement. Pre-tax deferrals through cafeteria plans are a type of compensation reduction agreement. Once the employee decides to convert their compensation into a payment of these benefits, the amount paid for these benefits through the employee’s pay is not deductible to a for-profit corporation. Under the new tax act, this appears to require tax exempt organizations pick up these amounts as taxable income and pay tax at the applicable corporate tax rates.

In summary, any situation where an employee receives a nontaxable qualified transportation benefit, whether paid by themselves through a payroll deduction, or provided by an employer who treats it as a nontaxable benefit to the employee, will create UBI to a tax exempt employer, which will be taxed at the regular corporate tax rates. Starting in 2018, the corporate tax rate will be a flat 21%. For those for-profit businesses, unless such benefits are included in employees’ payroll, these expenses will no longer be deductible.

Furthermore, regardless of when a business’ tax year-end is, these rules apply to amounts incurred or paid since January 1, 2018. Therefore, fiscal year-end tax exempt entities (i.e., 3/31/18 and 6/30/18) will need to plan on including these as UBI for the current year and will likely be required to file a 2017 Form 990-T and pay income tax using a blended tax rate. For-profit businesses will need to plan to modify payroll for employees who previously took advantage of these fringes.

ACTION STEPS

Every for-profit or tax exempt organization should examine its specific fact pattern to determine if any changes can be made to the benefit offering in order to mitigate negative tax consequences. In many cases, employers may choose to adapt their plan offerings to address the added tax costs. (It should be noted that in some jurisdictions, it is mandatory for certain sized companies to provide access to these tax-free benefits for their employees, which limits the ability to eliminate such a benefit if desired. For example, the District of Columbia requires any employer with more than 20 employees to provide either 1) an employee-paid pre-tax benefit, 2) an employer-paid direct benefit, or 3) employer-provided transportation.)
Identity Theft and Cybersecurity

As identity theft schemes become more complex, it is important for businesses and individuals to take appropriate measures to ensure assets are protected. Both businesses and individuals rely on technology that makes many aspects of their financial lives easier. However, this can also pave the way to exposing sensitive financial information to cybercriminals if security measures are not taken.

A common example of how cybercriminals steal data is by using phishing scams. Cybercriminals can pose as a data storage provider, bank, or the IRS, for example, by sending an urgent email and providing a link or attachment to resolve the purported issue. A nefarious link can deliver unsuspecting account owners to a fake bank site and prompt a log in to an account. Account owners would unwittingly be revealing their login credentials to cyberthieves.

Caution should be exercised when an unusual or suspicious email is received, even if it appears to come from someone familiar. Call the sender directly to verify that the email is safe.

Opening an attachment included with a phishing email is equally risky. In opening an attachment, malware may be downloaded, unleashing virus that can infect the user’s computer. It is important for businesses to train employees on how to recognize and avoid phishing scams. Suspicious IRS-related emails can be forwarded to phishing@irs.gov.

A tax-related identity theft is when a fraudulent tax return is filed with the IRS, using a stolen Social Security number to claim a fraudulent refund. This type of theft is often discovered when a taxpayer is notified by the IRS that a return was filed under their Social Security number. It is important to note that the IRS does not initiate contact with taxpayers by email, text messages, social media, or phone. Legitimate communications from the IRS are always received by mail on IRS letterhead.

ACTION STEPS

Taxpayers should take basic security measures to protect themselves against identity theft, including regularly monitoring their credit reports as well requesting tax transcripts to ensure that the records the IRS has on file are accurate.

In case of identity theft, taxpayers are advised to file a complaint with the Federal Trade Commission at www.identitytheft.gov and to contact one of the three major credit bureaus to place a “fraud alert” on your records. Taxpayers can request a credit freeze to stop any new accounts from being opened in their name. Form 14039, Identity Theft Affidavit, should also be mailed or faxed to the IRS to flag the taxpayer’s account for fraudulent activity. In the event that a resolution is not obtained with the IRS, a taxpayer can also contact the Identity Protection Specialist Unit at 1-800-908-4490.
A summary of the rules and potential tax impact to U.S. multinational companies under these provisions are discussed below.

**GLOBAL INTANGIBLE LOW-TAXED INCOME (“GILTI”)**

GILTI is essentially foreign income earned in the current year by a Controlled Foreign Corporation (“CFC”) in excess of an amount deemed to be a routine rate of return (i.e., 10%) on the CFC’s business assets. A CFC is a foreign corporation in which U.S. shareholder(s), in the collective, own more than 50% interest (vote or value) in such foreign corporation. For purposes of GILTI, the current year foreign income is reduced by any U.S. effectively connected income, other subpart F income, and deductions allocable to the CFC income, among other items. The resulting amount is referred to as the Net CFC Tested Income, and the excess of this amount over the Net Deemed Intangible Income Return, described below, constitutes the GILTI inclusion that is included in a U.S. shareholder’s gross income pro rata in the year earned. A U.S. shareholder is generally defined as a U.S. person with at least a 10% ownership (vote or value) in a foreign corporation.

The deemed rate of return mentioned above is termed as the Net Deemed Tangible Income Return under the GILTI provisions and is equal to 10% of the U.S. shareholder’s pro rata share of the CFC’s Qualified Business Asset Investment (“QBAI”). QBAI is defined as the quarterly average of the CFC’s tax basis in depreciable property used in a trade or business, over the amount of interest expense taken into account in determining such U.S. shareholder’s Net Tested CFC Income.

U.S. shareholders that are C-corporations are allowed a 50% deduction on their GILTI inclusion, resulting in a 10.5% effective tax rate (50% of the 21% corporate tax rate as of January 1, 2018). Additionally, corporate U.S. shareholders are also allowed a foreign tax credit on the GILTI inclusion, equal to 80% of such shareholder’s pro rata share of foreign income taxes attributable to the CFC income taken into account in determining the Net Tested CFC Income. As such, where the effective foreign tax rate on GILTI is 13.125% or higher, the corporate GILTI tax liability may be fully offset by the allowable foreign tax credits. It should be noted that foreign tax credit rules apply separately to foreign taxes paid on the GILTI and cannot be carried forward or carried back.

Starting with the 2018 tax year, U.S. shareholders of CFCs that do not have substantial amounts of depreciable assets as compared to their income, such as service companies and technology companies, may face a material tax burden as a result of the GILTI inclusion. Moreover, individual shareholders and pass-through entities owning stock in CFCs are not afforded the benefit of the 50% GILTI deduction or the reduced corporate tax rate of 21%. However, there may be planning strategies for mitigating such implications. It is highly advisable that the tax profile of each U.S. taxpayer be carefully reviewed to determine the most efficient strategy for U.S. tax purposes and to avoid unexpected adverse consequences.
FOREIGN-DERIVED INTANGIBLE INCOME ("FDII")

In addition to the GILTI rules discussed above, the international tax provisions enacted under the tax reform also included the FDII deduction. In a sense, the mechanics of determining the FDII deduction operate in a similar manner as the GILTI calculation; however, while a GILTI inclusion is generally a tax cost, a FDII deduction serves as a tax benefit.

The FDII deduction is available only to domestic corporations taxed as C-corporations for tax years beginning on or after January 1, 2018. It is essentially a deduction given on income earned by a domestic C-corporation selling property to foreign persons for foreign use, or for providing services to persons located outside the U.S. For purposes of determining FDII, "foreign use" means any use, consumption, or disposition which is not within the U.S. It should be noted that where the sale of property or the provision of services is to a related party, different rules may apply for purposes of the FDII deduction.

For purposes of calculating the FDII deduction, the first step is to determine the amount of income earned by the domestic C-corporation from the sale of property to foreign persons for foreign use, or for providing services to persons located outside the U.S. FDII excludes from the calculation certain types of income such as GILTI and other types of subpart F income, dividends received from CFCs, and any foreign branch income, among other items, and applies allocable deductions. Then the excess of this amount over the QBAI (10% of the corporation’s depreciable tangible property used in a trade or business, similar to GILTI) is multiplied by 37.5% to yield the FDII deduction amount in connection with the current year. The applicable rate for the FDII deduction is 37.5% for taxable years beginning after December 31, 2017, and before January 1, 2026, then will decrease to 21.875% for taxable years beginning after December 31, 2025.

ACTION STEPS

For GILTI:

▸ Individual U.S. shareholders may consider holding foreign entities through a domestic C-corporation to qualify for the 50% deduction on GILTI inclusion.

▸ For individual U.S. shareholders with controlled foreign entities in jurisdictions with high income tax rates, consider treating the foreign entities as pass-through entities to the extent possible, as this may maximize the use of foreign tax credits, resulting in a lower overall effective income tax rate.

▸ Please note there are certain types of entities in each foreign jurisdiction which are not eligible to be treated as pass-through entities for U.S. federal income tax purposes.

▸ Individual U.S. shareholders may consider making an annual election under IRC Section 962. Under this election, an individual would be treated as a corporation, enabling a foreign tax credit to be taken against any GILTI inclusion. However, the 50% GILTI deduction would not be available even with a Section 962 election, though the election may still be beneficial, provided the foreign income tax rates are high enough and profits are not repatriated regularly nor is there a plan for regular repatriation.

▸ It is recommended that a financial analysis be conducted to determine the potential tax impact of planning alternatives, as it relates to GILTI and other relevant considerations.

For FDII:

▸ Domestic C-corporations should examine transactions with foreign customers (for sales) and customers located outside the U.S. (for services) to determine the availability of the FDII deduction and to properly identify deductions allocable to this type of income.

▸ It is recommended that a financial analysis be conducted to determine the potential tax impact of planning alternatives, as it relates to the FDII deduction and other relevant considerations.
One of the main purposes of the reduction in the corporate tax rate was to make the U.S. competitive with foreign jurisdictions that offer lower tax rates and other tax incentives.
Transfer Pricing after Tax Reform

MAJOR CHANGES IN THE TAX ENVIRONMENT WILL AFFECT HOW MULTINATIONAL ENTITIES (“MNE’S”) STRUCTURE AND PRICE INTERCOMPANY TRANSACTIONS.

The Tax Cuts and Jobs Act of 2017 (“TCJA”) already is having both direct and indirect effects on global intercompany transactions. In addition, the implementation of certain action items proposed by the Organization for Economic Development (“OECD”) under the Base Erosion and Profit Shifting (“BEPS”) initiative, including Country by Country (“CBC”) reporting, are creating transparency with respect to global transfer pricing in a big way. Further, the Internal Revenue Service (“IRS”) is responding to these changes by issuing new directives to its employees on how transfer pricing examinations are to be conducted.

TCJA IMPACT ON TRANSFER PRICING
Several aspects of TCJA upended the way in which MNE’s will evaluate tax structuring and transfer pricing.

- **Corporate tax rate reduction.** One of the main purposes of the reduction in the corporate tax rate was to make the U.S. competitive with foreign jurisdictions that offer lower tax rates and other tax incentives. The reduction in the tax rate from 35%, formerly the fourth highest global tax rate, to 21% encourages MNE’s to re-evaluate the location of business activities, including the location of valuable intellectual property (IP) and the source of the performance of services such as research and development.

- **Global Intangible Low Taxed Income (“GILTI”).** This new tax applies to controlled foreign corporation (“CFC”) income that exceeds a 10% return on tangible assets. This tax only applies to CFCs and presents a new stand-alone anti-deferral regime. It applies in addition to the existing subpart F regime. Foreign tax credits can offset up to 80% of the GILTI tax. The GILTI tax was designed to discourage the offshoring of valuable IP as it taxes certain offshore income in a manner similar to the taxation of subpart F income. An indirect effect of the GILTI on transfer pricing is that it is based on a formulaic calculation that calls into question the traditional arm’s length principal used to evaluate the appropriateness of transfer pricing applied to intercompany transactions for MNE’s.

- **Foreign Derived Intangible Income (“FDII”).** Section 250 of the TCJA lowers the new 21% corporate tax rate to an effective rate of 13.125% for foreign-use intangibles held by U. S. taxpayers (“FDII eligible income”). FDII-eligible income relates to excess returns derived from foreign sources which include income from the sale of property, services provided, and licenses to non-U.S. entities/persons. The lower tax rate applicable to FDII income was designed to encourage U.S. entities to develop technology or intangibles in the U.S. and to license such IP to overseas affiliates. Further, it encourages U.S. entities to provide corporate support or other services to foreign affiliates. Similar to the GILTI, the indirect effect on transfer pricing is that the FDII calls into question the arm’s length principal used to evaluate the transfer pricing of MNE’s.

- **Base Erosion and Anti-Abuse Tax (“BEAT”).** The BEAT is a minimum tax charged on payments to related foreign affiliates. Like the former Corporate Alternative Minimum Tax (“AMT”), this is a parallel tax system that applies when the BEAT is in excess of the regular tax liability. Unlike the former corporate AMT, there is no credit to offset future regular tax liabilities. The BEAT specifically targets payments for services, royalties, and interest to foreign affiliates. The BEAT is calculated by increasing taxable income by deductions taken for related party transactions and taxing the modified taxable income at 5%. The BEAT only applies to MNE’s with revenues in excess of $500 million. Further, it only applies if payments to foreign affiliates equal or exceed 3% of total tax deductions. The direct impact of this tax is that it is aimed at transfer pricing payments made by U.S. entities to foreign related parties. It ignores traditional transfer pricing principles based upon the arm’s length method and seeks to broaden the tax base through the creation of a modified taxable income and taxed at a lower rate. Further, the BEAT potentially creates double taxation since transfer pricing examinations are based upon the calculation of the regular tax liability, and there is no mechanism for foreign entities to counteract the BEAT.
OECD BEPS INITIATIVE
As previously reported in this publication, the OECD published 15 action items addressing base erosion and profit shifting by taxpayers reporting in multiple taxing jurisdictions. The focus of these actions was to ensure that profits are taxed in the jurisdictions where they are earned. One of these action items introduced CBC reporting, which provides increased transparency of global transfer pricing. CBC reporting is required for MNE’s with global revenues in excess of $850 million. First-time implementation of this reporting occurred over the last year-and-a-half, as it was required in OECD members’ jurisdictions for tax years beginning after January 1, 2016, and for U.S.-reporting MNEs for tax years beginning after June 30, 2016, if not adopted earlier.

Similar to the OECD reporting template, Federal Form 8975 Country by Country Report is required to be attached to the U.S. tax return. Form 8975 discloses key information by the taxing jurisdiction including: unrelated party and related party revenues, profit or loss before income tax, income tax paid, income tax accrued, stated capital, accumulated earnings, number of employees, and tangible assets other than cash and cash equivalents. Disclosure of entities in each tax jurisdiction is required as well. This provides an increased level of transparency to tax examiners with regard to global intercompany transactions and an opportunity to identify base erosion and profit shifting occurring in the various tax jurisdictions.

NEW IRS DIRECTIVES FOR IRS TRANSFER PRICING EXAMINATIONS
The IRS Large Business and International ("LB&I") division released five directives on transfer pricing that impact the way that transfer pricing examinations are conducted. The new directives focus on:

► Elimination of the requirement that mandatory transfer pricing information document requests ("IDR’s") be issued;
► Appropriate application of the transfer pricing penalties as they apply to contemporaneous documentation;
► Analysis of the best method selection;
► The reasonably anticipated benefits in cost-sharing arrangements; and
► Cost-sharing arrangement stock-based compensation.

The integration and implementation of the five directives is aimed at creating more efficiency within the IRS during audit examinations. It also is an attempt to focus more closely on transfer pricing risk and reduce the number of transfer pricing audits conducted by the IRS. The first three of these directives have an impact for most MNEs. The latter two directives are more specific to cost-sharing arrangements and have limited application.

Although mandatory IDR’s will no longer be required to be issued at the beginning of an examination, there are certain cases when an IDR will be required. Taxpayers continue to be required to submit accurate documentation within 30 days of being issued an IDR, to prevent the possible application of penalties of 20 to 40 percent of any transfer pricing adjustment levied.

It would appear that LB&I IRS agents may experience fewer examinations than before the new IDR directive was implemented. However, the new IDR directive does not explicitly state that it exclusively applies to examinations of LB&I taxpayers (taxpayers with assets equal to or greater than $10 million). This leaves it open to interpretation and potentially means that middle-market companies with global operations may feel the effects of the new directive, in which case more transfer pricing examinations will occur.
ACTION STEPS

The TCJA changes related to the corporate tax rate and the imposition of FDII rules, GILTI, and the BEAT create a need to rethink the approach to transfer pricing and intangibles ownership. A thorough modeling of these changes needs to be performed by MNE taxpayers to determine the impact. Since this analysis is facts and circumstances-driven, there is no simple way to estimate the results or strategies that should be explored. Marcum recommends that MNE taxpayers undertake a study to determine the impact of the TCJA on international structuring, transfer pricing policies, and global tax rates.

The outcome of such a study will point out new strategies that should be explored to minimize global taxation for a MNE. Some possible new strategies could include:

► For FDII and GILTI, determine whether IP is better located in the U.S. or abroad, including the costs of unwinding current structures and implementing new structures.

► For GILTI:
  ► Maximize the exempt deemed tangible income returns on CFCs to minimize GILTI.
  ► Manage FTC.
  ► Manage PTI distributions.
  ► Consider non-CFC entities to house business operations, since the GILTI only applies to CFCs.

► For BEAT:
  ► Review mark-ups on payments to foreign related parties.
  ► Review licensing arrangements related to foreign related party IP.
  ► BEAT related party payments do not include cost of goods sold or services eligible for the Service Cost Method. Explore planning ideas related to these exceptions.

The CBC reporting and the new IRS directives related to transfer pricing should continue to be a focus for MNE tax departments. With transparency increased and an unknown factor as to whether an IDR will be issued for transfer pricing, MNE tax departments should continue to be diligent in preparing accurate contemporaneous documentation to provide penalty protection in the event of a transfer pricing adjustment upon examination. How transfer pricing audits will play out relative to the tax reform changes remains to be seen.

While all of these recent changes in the tax environment introduce new complexity to transfer pricing, they also create international tax and transfer pricing planning opportunities. Now is a time for not only large MNEs, but also small and mid-sized MNEs, to take a fresh look at their transfer pricing policies to identify new opportunities arising from U.S. tax reform.
### INFLATION/COST OF LIVING

#### TAX UPDATES

<table>
<thead>
<tr>
<th>TAX BENEFIT</th>
<th>2018</th>
</tr>
</thead>
<tbody>
<tr>
<td>Personal/Dependent Exemption</td>
<td>Suspended</td>
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</table>

#### STANDARD DEDUCTION

<table>
<thead>
<tr>
<th>Type</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Married Filing Joint</td>
<td>$24,000</td>
</tr>
<tr>
<td>Single</td>
<td>$12,000</td>
</tr>
<tr>
<td>Married Filing Separately</td>
<td>$12,000</td>
</tr>
<tr>
<td>Head of Household</td>
<td>$18,000</td>
</tr>
<tr>
<td>Foreign Earned Income Exclusion</td>
<td>$104,100</td>
</tr>
<tr>
<td>Maximum Taxable Social Security Earnings Base</td>
<td>$128,700</td>
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### HEALTH SAVINGS ACCOUNTS

#### CONTRIBUTION LIMITS

<table>
<thead>
<tr>
<th></th>
<th>2018</th>
<th>2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>Single/Family</td>
<td>$3,450/$6,900</td>
<td>$3,400/$6,750</td>
</tr>
<tr>
<td>Age 55+ Catch-Up</td>
<td>$1,000</td>
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### AMT EXEMPTION

#### PHASE-OUT THRESHOLDS

<table>
<thead>
<tr>
<th></th>
<th>2018</th>
<th>2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>Married Filing Jointly</td>
<td>$109,400</td>
<td>$1,000,000</td>
</tr>
<tr>
<td>Married Filing Separately</td>
<td>$54,700</td>
<td>$500,000</td>
</tr>
<tr>
<td>Single</td>
<td>$70,300</td>
<td>$500,000</td>
</tr>
</tbody>
</table>

Note: As AGI increases over a certain threshold, the AMT exemption is phased out.

### 2018 ESTATES AND TRUSTS TAX RATES

<table>
<thead>
<tr>
<th>OVER</th>
<th>BUT NOT OVER</th>
<th>THE TAX IS</th>
<th>OF THE AMOUNT OVER</th>
</tr>
</thead>
<tbody>
<tr>
<td>$2,550</td>
<td>$9,150</td>
<td>$255 + 24%</td>
<td>$2,550</td>
</tr>
<tr>
<td>$9,150</td>
<td>$12,500</td>
<td>$1,839 + 35%</td>
<td>$9,150</td>
</tr>
<tr>
<td>$12,501</td>
<td>-</td>
<td>$3,011.50 + 37%</td>
<td>$12,500</td>
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</table>

### 2018 INDIVIDUAL INCOME TAX RATES

<table>
<thead>
<tr>
<th>RATE</th>
<th>SINGLE</th>
<th>HEAD OF HOUSEHOLD</th>
<th>MARRIED-JOINT</th>
<th>MARRIED-SEPARATE</th>
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</thead>
<tbody>
<tr>
<td>10%</td>
<td>$0 - $9,525</td>
<td>$0 - $13,600</td>
<td>$0 - $19,050</td>
<td>$0 - $9,525</td>
</tr>
<tr>
<td>12%</td>
<td>$9,526 - $38,700</td>
<td>$13,601 - $51,800</td>
<td>$19,051 - $77,400</td>
<td>$9,526 - $38,700</td>
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<tr>
<td>22%</td>
<td>$38,701 - $82,500</td>
<td>$51,801 - $82,500</td>
<td>$77,401 - $165,000</td>
<td>$38,701 - $82,500</td>
</tr>
<tr>
<td>24%</td>
<td>$82,501 - $157,500</td>
<td>$82,501 - $157,500</td>
<td>$165,001 - $315,000</td>
<td>$82,501 - $157,500</td>
</tr>
<tr>
<td>32%</td>
<td>$157,501 - $200,000</td>
<td>$157,501 - $200,000</td>
<td>$315,001 - $400,000</td>
<td>$157,501 - $200,000</td>
</tr>
<tr>
<td>35%</td>
<td>$200,001 - $500,000</td>
<td>$200,001 - $500,000</td>
<td>$400,001 - $600,000</td>
<td>$200,001 - $300,000</td>
</tr>
<tr>
<td>37%</td>
<td>Over $500,001</td>
<td>Over $500,001</td>
<td>Over $600,001</td>
<td>Over $300,001</td>
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</table>
### Corporate Blended Rate for Fiscal Year Entities

<table>
<thead>
<tr>
<th>Fiscal Year Ended</th>
<th>Days in 2017</th>
<th>Days in 2018</th>
<th>% of Days in 2017</th>
<th>% of Days in 2018</th>
<th>Prorated Rate for 2017</th>
<th>Prorated Rate for 2018</th>
<th>Blended Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>January 31, 2018</td>
<td>334</td>
<td>31</td>
<td>92%</td>
<td>8%</td>
<td>32.0%</td>
<td>1.8%</td>
<td>33.8%</td>
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<tr>
<td>February 28, 2018</td>
<td>306</td>
<td>59</td>
<td>84%</td>
<td>16%</td>
<td>29.3%</td>
<td>3.4%</td>
<td>32.7%</td>
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<tr>
<td>March 31, 2018</td>
<td>275</td>
<td>90</td>
<td>75%</td>
<td>25%</td>
<td>26.4%</td>
<td>5.2%</td>
<td>31.5%</td>
</tr>
<tr>
<td>April 30, 2018</td>
<td>245</td>
<td>120</td>
<td>67%</td>
<td>33%</td>
<td>23.5%</td>
<td>6.9%</td>
<td>30.4%</td>
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<tr>
<td>May 31, 2018</td>
<td>214</td>
<td>151</td>
<td>59%</td>
<td>41%</td>
<td>20.5%</td>
<td>8.7%</td>
<td>29.2%</td>
</tr>
<tr>
<td>June 30, 2018</td>
<td>184</td>
<td>181</td>
<td>50%</td>
<td>50%</td>
<td>17.6%</td>
<td>10.4%</td>
<td>28.1%</td>
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<tr>
<td>July 31, 2018</td>
<td>153</td>
<td>212</td>
<td>42%</td>
<td>58%</td>
<td>14.7%</td>
<td>12.2%</td>
<td>26.9%</td>
</tr>
<tr>
<td>August 31, 2018</td>
<td>122</td>
<td>243</td>
<td>33%</td>
<td>67%</td>
<td>11.7%</td>
<td>14.0%</td>
<td>25.7%</td>
</tr>
<tr>
<td>September 30, 2018</td>
<td>92</td>
<td>273</td>
<td>25%</td>
<td>75%</td>
<td>8.8%</td>
<td>15.7%</td>
<td>24.5%</td>
</tr>
<tr>
<td>October 31, 2018</td>
<td>61</td>
<td>304</td>
<td>17%</td>
<td>83%</td>
<td>5.8%</td>
<td>17.5%</td>
<td>23.3%</td>
</tr>
<tr>
<td>November 30, 2018</td>
<td>31</td>
<td>334</td>
<td>8%</td>
<td>92%</td>
<td>3.0%</td>
<td>19.2%</td>
<td>22.2%</td>
</tr>
<tr>
<td>December 31, 2018</td>
<td>0</td>
<td>365</td>
<td>0%</td>
<td>100%</td>
<td>0%</td>
<td>21%</td>
<td>21.0%</td>
</tr>
</tbody>
</table>

### Dollar Limits for Retirement Plans

<table>
<thead>
<tr>
<th>Plan Types</th>
<th>2018 Limits</th>
</tr>
</thead>
<tbody>
<tr>
<td>Defined Contribution Plans</td>
<td>$55,000</td>
</tr>
<tr>
<td>Defined Benefit Plans</td>
<td>$220,000</td>
</tr>
<tr>
<td>Defined Contribution Plans – 401(k), 403(b) and 457 plans: Under Age 50</td>
<td>$18,500</td>
</tr>
<tr>
<td>Age 50 and older</td>
<td>$24,500</td>
</tr>
<tr>
<td>SIMPLE Plans: Under Age 50</td>
<td>$12,500</td>
</tr>
<tr>
<td>Age 50 and Older</td>
<td>$15,500</td>
</tr>
<tr>
<td>IRA, Traditional and Roth: Under Age 50</td>
<td>$5,500</td>
</tr>
<tr>
<td>Age 50 and Older</td>
<td>$1,000</td>
</tr>
<tr>
<td>IRA AGI Phase-Out (Married)</td>
<td>$101,000</td>
</tr>
<tr>
<td>IRA AGI Phase-Out (Single/HOH)</td>
<td>$63,000</td>
</tr>
</tbody>
</table>

### Other Thresholds

<table>
<thead>
<tr>
<th>2018 Limits</th>
</tr>
</thead>
<tbody>
<tr>
<td>SEP Annual Compensation Limit</td>
</tr>
<tr>
<td>Key Employee in a Top-Heavy Plan</td>
</tr>
<tr>
<td>Highly Compensated Employee</td>
</tr>
</tbody>
</table>

### Gift & Estate Tax Exemption

<table>
<thead>
<tr>
<th>2012</th>
<th>2013</th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
<th>2017</th>
<th>2018*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gift Tax Exemption</td>
<td>$5,120,000</td>
<td>$5,250,000</td>
<td>$5,340,000</td>
<td>$5,430,000</td>
<td>$5,450,000</td>
<td>$5,490,000</td>
</tr>
<tr>
<td>Estate Tax Exemption</td>
<td>$5,120,000</td>
<td>$5,000,000</td>
<td>$5,340,000</td>
<td>$5,430,000</td>
<td>$5,450,000</td>
<td>$5,490,000</td>
</tr>
<tr>
<td>GST Tax Exemption</td>
<td>$5,120,000</td>
<td>$5,250,000</td>
<td>$5,340,000</td>
<td>$5,430,000</td>
<td>$5,450,000</td>
<td>$5,490,000</td>
</tr>
<tr>
<td>Highest Estate &amp; Gift Tax Rates</td>
<td>35%</td>
<td>40%</td>
<td>40%</td>
<td>40%</td>
<td>40%</td>
<td>40%</td>
</tr>
</tbody>
</table>

*Annual Gift Exclusion is $15,000
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