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# Federal tax overhaul creates uncertainty, hope for business owners

More than 30 years after digesting the last major federal tax overhaul, Connecticut accountants and legal advisers working to interpret the latest changes to the federal tax code say business clients are both enthusiastic and wary as they figure out how to adapt.

Sweeping changes are at hand for businesses ranging from large conglomerates like United Technologies Corp. (UTC) to small mom-and-pop shops like a Fairfield jeweler, and everyone in between.

"You really have to make sure you look to the future," said Patrick Duffany, managing partner for tax services at CohnReznick in Hartford. "The wrong call could create costs to unwind what you have done, or require you to pay a tax cost you could have avoided."

Mark Everson of the Washington, D.C.-based specialty tax services firm the alliantgroup, recently told a Cromwell forum, sponsored by his firm and BlumShapiro and put on by the Connecticut Business & Industry Association, that the last significant changes to the federal tax code happened in 1986.

"The media has created so much attention, business clients are craving information," said Brett McGrath, the partner in charge of accounting firm Marcum's Connecticut tax services.

In addition to constant email blasts about the latest tax changes, Marcum held three days of webinars at the end of January for its clients, McGrath said.

The biggest changes introduced by the Tax Cuts and Jobs Act of 2017 that primarily affect businesses involve a 20 percent deduction for pass-through companies; mandatory repatriation of not only current foreign earnings but those going back 30 years (but at a lower rate of 15.5 percent); and a decline in the corporate tax rate from 35 percent to 21 percent, advisers said.

In addition, advisers said the state and local income tax (SALT) deduction, which has a new $10,000 limit for individual taxpayers, may drive some senior management executives out of state. Connecticut and 11 other states plan to argue in federal court that the deduction cap is unconstitutional.

Gov. Dannel P. Malloy said the law will cost Connecticut taxpayers billions in deductions. He's also proposing potential workarounds.

More guidance needed

Even though President Donald Trump signed the law in December, guidance and regulations from the Internal Revenue Service are not yet available in most cases.

Complicating matters further, adds Greg Cabral, managing partner in BlumShapiro's Rhode Island office, is the fact that some states, including Connecticut, haven't yet adopted the 20 percent pass-through deduction. And because it would cost some states tax revenues, Connecticut, which is still running a deficit, likely won't, he said.

A Malloy spokesman said the governor is not proposing adoption of the deduction, but he'd work with lawmakers if they wanted to. He has, however, proposed tax changes to pass-through entities aimed at allowing them to reduce their federal income tax liability.

Malloy also said Connecticut will not adopt federal tax changes related to accelerated depreciation and asset expensing, which would cost the state money.

Given the uncertainty, many accountants said their business clients are approaching the changes with "cautious optimism" — embracing the tax provisions that have clear advantages in their given situation, but taking a "wait-and-see" approach to major adaptations they have to research and analyze, like restructuring a business, which could have long-term consequences.

Advisers said their clients are not confused so much as concerned — especially small businesses that do not have in-house tax advisers.

The "biggest buzz" is coming from the 20 percent deduction for pass-through companies, which is complicated, said Andrew Lattimer, a BlumShapiro tax partner in West Hartford.

Pass-through taxation applies to sole proprietorships, partnerships and S-corporations — entities in which the owners, as shareholders, partners or LLC members, pay the tax, Lattimer said.

Pass-through companies do not include C-corporations, where there's double taxation because the tax is paid both at the corporate and ownership level, Lattimer said.

Service companies like accounting and law firms won't get the deduction, but manufacturers, construction, engineering and architecture firms will, he said.

Also, to qualify for the full deduction, taxable income must be below $157,500 for a single filer and $315,000 for joint filers.

"I've had quite a few business owners tell me that they thought they were going to pay more until I ran the numbers for them, and they saw they'll pay less and were pleasantly surprised," Lattimer said.

There is some confusion, added McGrath of Marcum, regarding how to determine what constitutes so-called "qualified income," the amount upon which the deduction is based.

## SALT impact

The 20-percent deduction on pass-through companies is one reason Harry French, board chairman for Fairfield-based Henry C. Reid & Sons Jewelers, is considering restructuring from a C-corp to an LLC.

French said the restructuring is also a reaction to the $10,000 state and local tax deduction cap, which many of his wealthy jewelry clients are complaining about.

"I've got customers with literally dozens of homes on the water where they're paying $40,000, $50,000 or more in taxes that they won't be able to write off anymore," French said. "That affects my customers. And if it affects my customers, it will also affect me."

Local tax advisers said the $10,000 SALT deduction limit could drive C-suite executives out of state, if not for the full year then long enough to be considered out-of-state residents.

"I think [the SALT provision] is going to accelerate folks who can afford it, leaving the state for six months and a day," said Robert Karn, a principal with Farmington accounting firm Karn Couzens.

Malloy said 41 percent of Connecticut taxpayers use SALT deductions (averaging $18,939.72). He recently proposed a potential SALT cap workaround, but it's not clear if it will pass legal muster.

His proposal would allow cities and towns to create charitable organizations that provide government services. Taxpayers could make contributions to the charities, avoiding local tax payments, and then claim a charitable deduction, which isn't capped.

## UTC's perspective

Meantime, large companies like UTC are embracing the corporate tax rate reduction and the repatriation of earnings to the U.S.

Elizabeth Coffin, UTC's vice president for global tax policy, said the conglomerate, whose subsidiaries include Pratt & Whitney and Otis Elevator, had spent years advocating for a more competitive tax code.

Though still evaluating the impact of the new law, UTC is eagerly tuning in to upcoming "interpretive guidance" from federal agencies, she said.

UTC Chairman and CEO Gregory Hayes told CNBC recently that the company plans to repatriate this year $3 billion in overseas cash, a much higher amount than usual, thanks to the tax law. Some of that money will help pay down debt from the company's pending $23 billion purchase of Rockwell Collins.