WHAT TAX CHANGES ARE IN STORE FOR 2018?

We hope 2018 has started off well for you! This month we thought the tax topic was appropriate to review again with some helpful tips for small businesses. As you know, the tax reform bill became law, but of course that applies to 2018 and beyond. This month’s article focuses on some different things to be watching for in 2018 under the new law that may come into play for you right away as you plan your year. We encourage you to work with your accountant to keep up on the latest guidance that may affect your business.

Best Regards,

Keith Knudsen
President/CEO
Security Bank

2018 TAX REFORM LAW HAS BENEFITS FOR SOME SMALL BUSINESSES

by Ken Berry, CPA Practice Advisor Tax Correspondent
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The monumental new tax law signed late in 2017 – the Tax Cuts and Jobs Act (TCJA) – has been hailed as a boon for big business. But the TCJA also benefits many small businesses while presenting new obstacles. In general, the revised rules for businesses take effect in 2018 and are permanent, unlike most changes for individuals. Following are the key provisions likely to affect small businesses.

Corporate taxation: The graduated tax rate structure for corporations, featuring a top tax rate of 35%, is being replaced by a flat rate of 21%. As a result, the overall tax liability of many C corporations will be reduced. Furthermore, cash accounting was generally not available to corporations with average gross receipts for the three prior years of $5 million or more. This rule has been replaced by a $25 million gross receipts test.

Section 179 deductions: Under Section 179 of the Internal Revenue Code, a business could expense up to $500,000 of the cost of qualified business property,
subject to a dollar-for-dollar phaseout above $2 million. These figures were indexed for inflation. The new law doubles the maximum allowance to $1 million and increases the phaseout threshold to $2.5 million. Caveat: The maximum allowance is still limited to the amount of income from business activity.

**Bonus depreciation:** In recent years, the percentage for first-year “bonus depreciation” deductions has fluctuated, complicating tax planning. Now the new law hikes the bonus depreciation deduction from 50% to 100% for five years and then gradually phases out the deduction over the next five years. Added bonus: The deduction has been expanded to include “used” property that otherwise qualifies under this provision.

**Luxury car deductions:** The annual depreciation limits for “luxury cars” kick in at surprisingly modest levels. Now the new law hikes the limits for business drivers for cars placed in service in 2018 and thereafter. For instance, not even counting bonus depreciation, the first-year deduction jumps from $3,160 to $10,000. Of course, actual deductions must be based on percentage of business use.

**Pass-through entities:** The net income of pass-through entities like partnerships, S corporations, limited liability companies (LLCs) and sole proprietors is effectively taxed at individual tax rates. Now, for the first time ever, the new law creates a 20% deduction on income for pass-through entities, subject to certain limitations. Notably, the deduction only applies to “qualified business income” and can't be claimed by taxpayers in service businesses (excluding architecture and engineering) for single filers with taxable income above $157,500, and $315,000 for joint filers.

**Other deductions and credits:** Finally, the new law includes a slew of other changes affecting deductions and credits commonly claimed by businesses. For instance:

- The Section 199 deduction for qualified domestic property activities is repealed. This deduction was most often claimed by manufacturing firms.
- The new law revamps the rules for net operating losses (NOLs). Essentially, NOLs can no longer be carried back for two years, but can now be carried forward indefinitely (instead of for 20 years), subject to a limit of 80% of taxable income.
- The deduction for entertainment expenses that are directly-related-to or associated-with the conduct of business are repealed.
- The deduction for transportation fringe benefits – including mass transit passes, commuter vehicles and parking privileges – are repealed. If employers still provide these benefits, they remain tax-free to employees.
- The new law reduces the deduction for on-site eating facilities like cafeterias from 100% to 50% before it disappears completely after 2025. But this fringe benefit remains tax-free to employees.
- The deduction for business interest expenses is generally capped at 30% of adjusted taxable income, among other requirements. However, a small business with annual average gross receipts of $25 million or less for the past three years is exempt from this rule.
- The TCJA creates a new tax credit of employer-paid wages paid for family or medical leave. The credit can range from 12.5% to 25%, depending on the amount paid. But this credit disappears after 2019.
- Finally, the new law completely revamps the international tax system, including a repatriation tax on profits earned overseas.

In the wake of these changes, small business clients may seek your assistance in 2018.

In particular, planning may focus on the new deduction for pass-through entities. These rules are so complex even tax experts are having trouble sorting through them, but some clients may be tempted to shift the form of business ownership or transfer ownership shares to other family members to cash in on this tax break.

Expect the IRS to issue guidance on the new deduction for pass-through entities and other aspects of the new tax law affecting small businesses. We will continue to update you on significant new developments.

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