Understanding How the TCJA Will Affect Your Business

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AGENDA

- Overview of Changes
- Quick Review of Basic Entity Structures
- Changes for Businesses
- Opportunities for Businesses

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THE BASICS

Overview Changes

The Tax Cuts and Jobs ACT (TCJA) contains the most substantial changes to the tax code we have seen in over 30 years.

The intended outcome of this tax reform was to lower taxes for all individual and corporate tax payers, so that money would pour back into the economy.

- Individual and corporate tax changes are effective January 1, 2018, but many individual provisions expire December 31, 2025.
- Qualifying pass-through entity and sole proprietor business income for individuals (and estates and trusts) generally has a 20% deduction.
- Corporate income tax rates are reduced to 21% (from 35%) and the corporate AMT is repealed.

Source: IRS.gov

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Taxpayers Defined

Taxpayer Types

- Individuals
- Business Entities

Sole Proprietors *Partnerships* *LLC's*

C-Corporations *S-Corporations*

- Trusts
- Estates

Source: IRS.gov

C-Corporation Basics

Any corporation can be taxed as a C-corporation.

A C-corporation pays corporation taxes on its profits.

Shareholders pay personal income tax on dividends received.

Double taxation of dividends a disadvantage of C-corporations.

Advantages:

- Enhanced credibility among suppliers and lenders.
- Unlimited growth potential.
- No limit on number of shareholders (though once the company reached certain thresholds, it is required to register with the SEC under the Securities Exchange Act of 1934).
- Ability to reinvest profits in the company at a lower corporate tax rate.

Source: IRS.gov

Pass Through Basics

To qualify for S corporation status, the corporation must meet the following requirements:

- Be a domestic corporation
- Have only allowable shareholders
  - May be individuals, certain trusts or estates and
  - May not be partnerships, corporations or non-resident alien shareholders
- Have no more than 100 shareholders
- Have only one class of stock
- Not be an ineligible corporation (i.e. certain financial institutions, insurance companies, and domestic international sales corporations)

Source: IRS.gov

Pass Through Basics: S-Corporations

- S-corporations are corporations that elect to pass corporate income, losses, deductions, and credits through to their shareholders for federal tax purposes.
- Shareholders of S-corporations report the flow-through of income and losses on their personal tax returns and are assessed tax at their individual income tax rates.
- S-corporations to avoid double taxation on the corporate income.
- S-corporations are responsible for tax on certain built-in gains and passive income at the entity level.

Source: IRS.gov

Pass Through Basics: LLCs

Disregarded Entity

- Can elect this form of taxation for a single individual/trust or a married couple/trust.
- Income reported on Schedule C of personal tax return

Partnership

- Each partner shares in profits and losses of the business.
- A partnership must file an annual information return to report the income, deductions, gains, losses, etc., from its operations, but it does not pay income tax.
- Income passes through profits or losses to its partners.
- Partners are not employees and should not be issued a Form W-2. The partnership must furnish copies of Schedule K-1 (Form 1065) to the partners by the date Form 1065 is required to be filed, including extensions. Income then reported on individual partner's return (Schedule E)

S-Corporation

Source: IRS.gov

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THE CHANGES - Businesses

Tax Cut and Jobs Act

Tax Cut and Jobs Act of 2018

- Lowers C Corporation tax bracket to 21% from 35%
- Allows some owners of pass-through entities to deduct 20% of Qualified Business Income*
- Business tax cuts permanent

Source: AXA Split Dollar 2018 Presentation

Opportunities for Business Owners

C CORP

- “Cost” of key person and non-qualified executive benefit plans will be less
- Personal bracket may be higher than corporate bracket so a split dollar plan may make sense
- Lower personal rates mean more after tax income available to meet personal goals

PASS THROUGH ENTITY (S CORP, LLC, PARTNERSHIP)

- Lower tax on pass-through earnings make employer-owned executive benefit plans more attractive
- Lower personal rates mean more after tax income available to meet personal goals

Source: AXA Split Dollar 2018 Presentation

Qualified Business Income Deduction - Section 199A

Are you single with income less than $157,500?

→ You get full 20% QBI deduction

Are you a joint filer with joint income less than $315,000?

→ You get the full 20% QBI deduction

Qualified Business Income Deduction - Section 199A

What if your income is higher than $157,500 single or $315,000 joint?

If your business is not a specialized trade or service business, you can take a QBI deduction equal to the or less than the greater of:

1) 50% of W-2 wages paid
2) 25% of the W-2 wages paid by the business plus 2.5% of the unadjusted basis of depreciable property

Qualified Business Income Deduction - Section 199A

Specified Service Business

- Doctors
- Lawyers
- CPAs
- Financial Advisors
- Athletes
- Musicians
- Any business in which the principal asset of the business is the skill of reputation of one or more of its employees

Qualified Business Income Deduction - Section 199A

What if your income is higher than $157,500 single or $315,000 joint and you are a specified service business:

Phase out range for single filers $50,000 - $207,500

Phase out range for joint filers $100,000 - $415,000

Reduce Your Income

QBI Deduction Strategies

SUMMARY OF QBI DEDUCTION STRATEGIES

Income Reduction Strategies	Revisit filing separate returns for married couples	Beef up retirement plan contributions (especially at or close to phase-out ranges)	Transfer portions of ownership to various non-grantor trusts	Manage portfolio income	Consider passing on bonus depreciation to lower income in multiple years	Hire children for bone fide work	Consider donor-advised funds and other strategies to lower taxable income
"Income Alchemy" Strategies	Spin-off business-owned real estate into a separate entity and lease-back the property	Spin-off business owned depreciable equipment/property into a separate entity lease-back to equipment/property	Create an employee leasing company. Contract with the employee leasing company to provide staff	Avoid celebrity and high-profile employees	Avoid marketing language that makes strong claims about a business owner's skills		
Business Decisions	Switch from salaried employee to independent contarctor	Reduce independent contract labor in favor of hiring more W-2 employees	Converting non-salary-paying sole proprietors, LLCs, or partnerships, into S corporations	Change profit-eligible-only S corporations to partnerships	Reduce or eliminate guaranteed payments to partners		

Opportunities for Business Owners

- There will be a strong movement away from pass through entities to C-Corporations
- This will be due to the differential and potential arbitrage between lower corporate taxes and individual maximum taxes with deductions significantly curtailed

Source: AXA Split Dollar 2018 Presentation

Opportunities for Business Owners

Additional funds for:

- Profits
- Investment in business
- Employee base compensation
- Funding qualified retirement accounts
- Non-qualified Employer deferred compensation
- Non-qualified employee incentive compensation
- Long term care insurance

Source: AXA Split Dollar 2018 Presentation

Opportunities for Business Owners – Qualified Plan

THE THREE MAIN QBI DEDUCTION STRATEGY BUCKETS

	Income Reduction Strategies	"Income Alchemy" Strategies	Business Strategies
OBJECTIVE	Stay below the income threshold where the specified service business or wage-and-property tests kick in.	Transform income from a specified service business into income from a non-specified service business.	Favorably characterize business income.
METHOD	• Increase deductions • Spread income out over multiple taxpayers	• Spin off then lease-back certain assets • Avoid strong claims about business owner's skill	• Change an entity • Revisit compensation model • Revisit business assets

Opportunities for Business Owners

Long Term Care

- Can be provided on a discriminatory basis
- Premiums tax deductible to Corp
- Premiums not reportable income to employee
- Premium not reportable to owner of a C-Corp
- Benefits income tax free
- Join us for a future work shop dedicated to long term care solutions

Source: AXA Split Dollar 2018 Presentation

THANKS!
Any questions?

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