2018 Tax Reform: What You Need to Know Now

Dallas CPA Society – Member Appreciation CPE Series
Transaction Approach to Tax Reform

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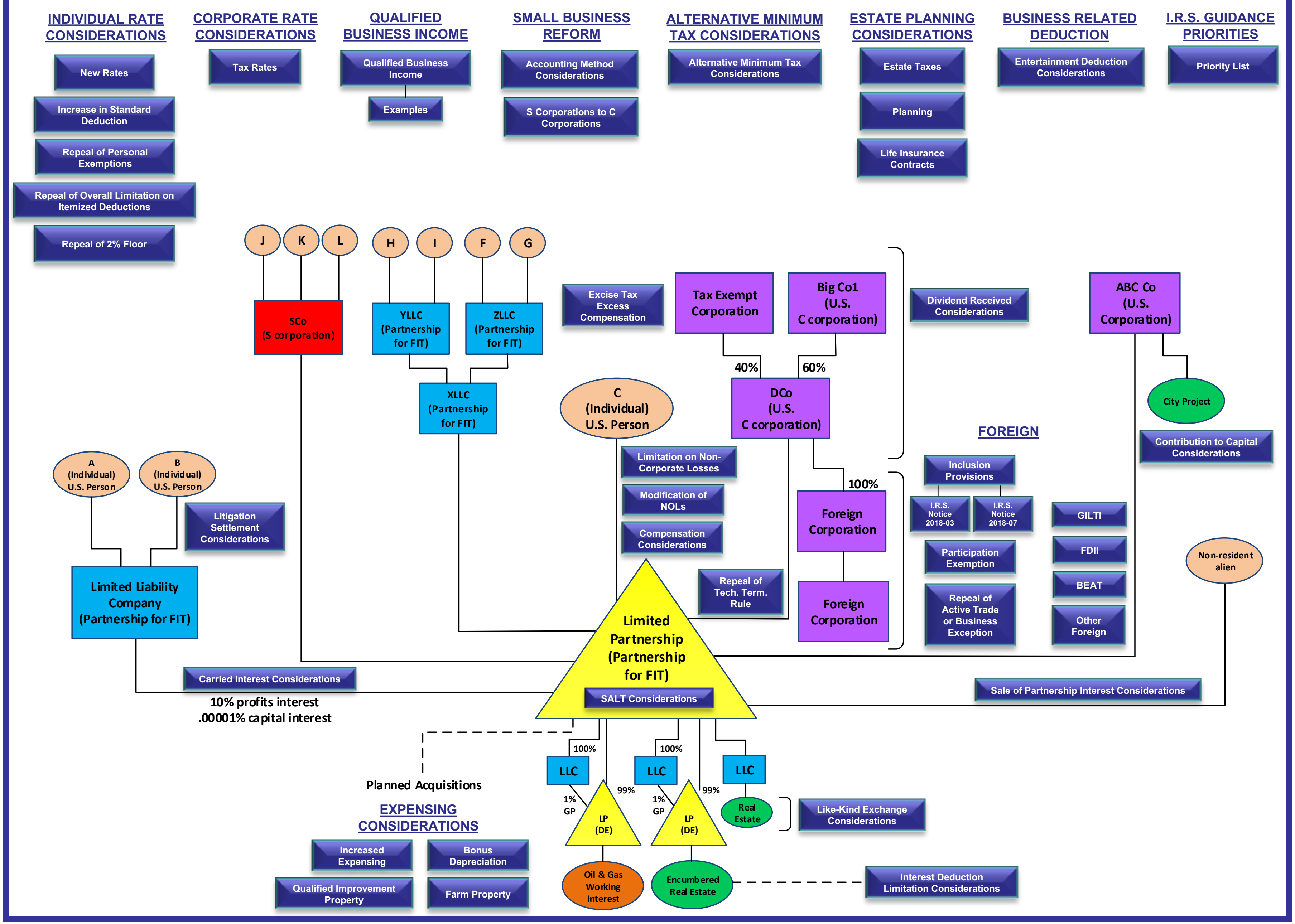
Selected Partnership Structural Considerations Arising from Tax Reform Process



A – INDIVIDUAL RATE STRUCTURE

The Act temporarily replaces the existing rate structure with a new rate structure.

If taxable income is:	Then income tax equals:
Single Individuals	
Not over $9,525	10% of the taxable income
Over $9,525 but not over $38,700	$952.50 plus 12% of the excess over $9,525
Over $38,700 but not over $82,500	$4,453.50 plus 22% of the excess over $38,700
Over $82,500 but not over $157,500	$14,089.50 plus 24% of the excess over $82,500
Over $157,500 but not over $200,000	$32,089.50 plus 32% of the excess over $157,500
Over $200,000 but not over $500,000	$45,689.50 plus 35% of the excess over $200,000
Over $500,000	$150,689.50 plus 37% of the excess over $500,000
Heads of Households	
Not over $13,600	10% of the taxable income
Over $13,600 but not over $51,800	$1,360 plus 12% of the excess over $13,600
Over $51,800 but not over $82,500	$5,944 plus 22% of the excess over $51,800

[1] I.R.C. § 1(j)(2)(C).
[2] I.R.C. § 1(j)(2)(B).

A - INDIVIDUAL RATE STRUCTURE

If taxable income is:	Then income tax equals:
Over $82,500 but not over $157,500	$12,698 plus 24% of the excess over $82,500
Over $157,500 but not over $200,000	$30,698 plus 32% of the excess over $157,500
Over $200,000 but not over $500,000	$44,298 plus 35% of the excess over $200,000
Over $500,000	$149,298 plus 37% of the excess over $500,000
Married Individuals Filing Joint Returns and Surviving Spouses	
Not over $19,050	10% of the taxable income
Over $19,050 but not over $77,400	$1,905 plus 12% of the excess over $19,050
Over $77,400 but not over $165,000	$8,907 plus 22% of the excess over $77,400
Over $165,000 but not over $315,000	$28,179 plus 24% of the excess over $165,000
Over $315,000 but not over $400,000	$64,179 plus 32% of the excess over $315,000
Over $400,000 but not over $600,000	$91,379 plus 35% of the excess over $400,000
Over $600,000	$161,379 plus 37% of the excess over $600,000
Married Individuals Filing Separate Returns	
Not over $9,525	10% of the taxable income
Over $9,525 but not over $38,700	$952.50 plus 12% of the excess over $9,525
Over $38,700 but not over $82,500	$4,453.50 plus 22% of the excess over $38,700
Over $82,500 but not over $157,500	$14,089.50 plus 24% of the excess over $82,500
Over $157,500 but not over $200,000	$32,089.50 plus 32% of the excess over $157,500
Over $200,000 but not over $300,000	$45,689.50 plus 35% of the excess over $200,000
Over $300,000	$80,689.50 plus 37% of the excess over $300,000
	Estates and Trusts
Not over $2,550	10% of the taxable income
Over $2,550 but not over $9,150	$255 plus 24% of the excess over $2,550
Over $9,150 but not over $12,500	$1,839 plus 35% of the excess over $9,150
Over $12,500	$3,011.50 plus 37% of the excess over $12,500

[1] I.R.C. § 1(j)(2)(A).
[2] I.R.C. § 1(j)(2)(D).
[3] I.R.C. § 1(j)(2)(E).

A.1. - REDUCTION IN CORPORATE TAX RATE

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
<u>In general</u> Corporate taxable income is subject to tax under a four-step graduated rate structure. The top corporate tax rate is 35 percent on taxable income in excess of $10 million. The corporate taxable income brackets and tax rates are as set forth in the table below. CLICK HERE FOR CHART An additional five-percent tax is imposed on a corporation's taxable income in excess of $100,000. The maximum additional tax is $11,750. Also, a second additional three-percent tax is imposed on a corporation's taxable income in excess of $15 million. The maximum second additional tax is $100,000. Certain personal service corporations pay tax on their entire taxable income at the rate of 35 percent. Present law provides that, if the maximum corporate tax rate exceeds 35 percent, the maximum rate on a corporation's net capital gain will be 35 percent. **<u>Dividends received deduction</u>** Corporations are allowed a deduction with respect to dividends received from other taxable domestic corporations. The amount of the deduction is generally equal to 70 percent of the dividend received. In the case of any dividend received from a 20-percent owned corporation, the amount of the deduction is equal to 80 percent of the dividend received. The term "20-percent owned corporation" means any corporation if 20 percent or more of the stock of such corporation (by vote and value) is owned by the taxpayer. For this purpose, certain preferred stock is not taken into account.	**1. New Corporate Rate Structure.** The provision eliminates the graduated corporate rate structure and instead taxes corporate taxable income at 21 percent.[1] Special rules apply to taxpayers subject to the normalization method of accounting. **2. Reduction in Dividends Received Deduction.** The provision reduces the 70 percent dividends received deduction to 50 percent[2] and the 80 percent dividends received deduction to 65 percent.[3] [1] I.R.C. § 11(b). [2] I.R.C. § 243(a)(1). [3] I.R.C. § 243(c)(1). [4] Act Sec. 13002(f).	The provision applies to taxable years beginning after December 31, 2017.[4]	§ 11 § 243

A.1. - REDUCTION IN CORPORATE TAX RATE

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
In the case of a dividend received from a corporation that is a member of the same affiliated group, a corporation is generally allowed a deduction equal to 100 percent of the dividend received.			§ 11 § 243

Tax Reform
Section B

B.1. – BONUS DEPRECIATION

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
A taxpayer generally must capitalize the cost of property used in a trade or business or held for the production of income and recover such cost over time through annual deductions for depreciation or amortization. **<u>Tangible property</u>** Tangible property generally is depreciated under the modified accelerated cost recovery system ("MACRS"), which determines depreciation for different types of property based on an assigned applicable depreciation method, recovery period, and convention. **<u>Bonus depreciation</u>** An additional first-year depreciation deduction is allowed equal to 50 percent of the adjusted basis of qualified property acquired and placed in service before January 1, 2020 (January 1, 2021, for longer production period property and certain aircraft). The 50-percent allowance is phased down for property placed in service after December 31, 2017 (after December 31, 2018 for longer production period property and certain aircraft). The bonus depreciation percentage rates are as follows. CLICK HERE FOR CHART The additional first-year depreciation deduction is allowed for both the regular tax and the alternative minimum tax ("AMT"), but is not allowed in computing earnings and profits. The basis of the property and the depreciation allowances in the year of purchase and later years are appropriately adjusted to reflect the additional first-year depreciation deduction. The amount of the additional first-year depreciation deduction is not affected by a short taxable year. The	**1. Full expensing for certain business assets.** a. **Extension and Modification of First-Year Depreciation Deduction.** The provision extends and modifies the additional first-year depreciation deduction through 2026 (through 2027 for longer production period property and certain aircraft).[1] The 50-percent allowance is increased to 100 percent for property placed in service after September 27, 2017, and before January 1, 2023[2] (January 1, 2024, for longer production period property and certain aircraft[3]), as well as for specified plants planted or grafted after September 27, 2017, and before January 1, 2023.[4] b. **Maintenance of Present Law Phase Down Rules.** The present-law phase-down of bonus depreciation is maintained for property acquired before September 28, 2017, and placed in service after September 27, 2017, as well as the present-law phase-down of the section 280F increase amount in the limitation on the depreciation deductions allowed with respect to certain passenger automobiles acquired before September 28, 2017, and placed in service after September 27, 2017. The section 280F increase amount in the limitation on the depreciation deductions allowed with respect to certain passenger automobiles acquired before September 28, 2017, and placed in service after September 27, 2017, is $8,000 for 2017, $6,400 for 2018, and $4,800 for 2019.[5]	The provision generally applies to property acquired and placed in service after September 27, 2017,[40] and to specified plants planted or grafted after such date.[41] Property is not treated as acquired after the date on which a written binding contract is entered into for such acquisition.[42]	§ 168(k)

B.1. – BONUS DEPRECIATION

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
taxpayer may elect out of the additional first-year depreciation for any class of property for any taxable year. The interaction of the additional first-year depreciation allowance with the otherwise applicable depreciation allowance may be illustrated as follows. Assume that in 2017 a taxpayer purchases new depreciable property and places it in service. The property's cost is $10,000, and it is five-year property subject to the 200 percent declining balance method and half-year convention. The amount of additional first-year depreciation allowed is $5,000. The remaining. $5,000 of the cost of the property is depreciable under the rules applicable to five-year property. Thus, $1,000 also is allowed as a depreciation deduction in 2017. The total depreciation deduction with respect to the property for 2017 is $6,000. The remaining $4,000 adjusted basis of the property generally is recovered through otherwise applicable depreciation rules. **Qualified property** Property qualifying for the additional first-year depreciation deduction must meet all of the following requirements. First, the property must be: (1) property to which MACRS applies with an applicable recovery period of 20 years or less; (2) water utility property; (3) computer software other than computer software covered by section 197; or (4) qualified improvement property. Second, the original use of the property must commence with the taxpayer. Third, the taxpayer must acquire the property within the applicable time period (as described below). Finally, the property must be placed in service before January 1, 2020. As noted above, an extension of the placed-in-service date of one year (i.e., before January 1, 2021) is provided for certain property with a recovery period of 10 years or longer, certain transportation property, and certain aircraft.	2. **Bonus Depreciation Rates.** Under the provision, in the case of property acquired and adjusted basis incurred before September 28, 2017, the bonus depreciation rates are listed in the following chart:: CLICK HERE FOR CHART 3. **Special Rules.** a. **Application to Used Property.** The Act removed the requirement that the original use of qualified property must commence with the taxpayer (*i.e.*, it allows the additional first-year depreciation deduction for new and used property).[28] To prevent abuses, the additional first-year depreciation deduction applies only to property purchased in an arm's-length transaction. The provision applies only if the property was not used by the taxpayer at any time prior to acquisition.[29] It does not apply to property received as a gift or from a decedent.[30] In the case of trade-ins, like-kind exchanges, or involuntary conversions, it applies only to any money paid in addition to the traded-in property or in excess of the adjusted basis of the replaced property.[31] It does not apply to property acquired in a nontaxable exchange such as a reorganization, to property acquired from a member of the taxpayer's family, including a spouse, ancestors, and lineal descendants, or from another related entity as defined in Section 267, nor to property acquired from a person who controls, is controlled by, or is under common control with, the taxpayer.[32] Thus it does not apply, for example, if one member of an affiliated group of corporations purchases property from another member, or if an individual who controls a corporation purchases property from that corporation.[33]		§ 168(k)

B.1. – BONUS DEPRECIATION

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
To qualify, property must be acquired (1) before January 1, 2020, or (2) pursuant to a binding written contract which was entered into before January 1, 2020. With respect to property that is manufactured, constructed, or produced by the taxpayer for use by the taxpayer, the taxpayer must begin the manufacture, construction, or production of the property before January 1, 2020. Property that is manufactured, constructed, or produced for the taxpayer by another person under a contract that is entered into prior to the manufacture, construction, or production of the property is considered to be manufactured, constructed, or produced by the taxpayer. For property eligible for the extended placed-in-service date, a special rule limits the amount of costs eligible for the additional first-year depreciation. With respect to such property, only the portion of the basis that is properly attributable to the costs incurred before January 1, 2020 ("progress expenditures") is eligible for the additional first-year depreciation deduction. **<u>Qualified improvement property</u>** Qualified improvement property is any improvement to an interior portion of a building that is nonresidential real property if such improvement is placed in service after the date such building was first placed in service. Qualified improvement property does not include any improvement for which the expenditure is attributable to the enlargement of the building, any elevator or escalator, or the internal structural framework of the building.	**2. Repeal of Election to Accelerate AMT Credits.** As a conforming amendment to the repeal of corporate AMT, the conference agreement repeals the election to accelerate AMT credits in lieu of bonus depreciation.[34] **3. Transitional Rule Election to Apply 50-Percent Allowance.** A transition rule provides that, for a taxpayer's first taxable year ending after September 27, 2017, the taxpayer may elect to apply a 50-percent allowance instead of the 100- percent allowance.[35] **D. Application to qualified film, television and live theatrical productions.** The provision expands the definition of qualified property eligible for the additional first-year depreciation allowance to include qualified film, television and live theatrical productions placed in service after September 27, 2017, and before January 1, 2027, for which a deduction otherwise would have been allowable under section 181 without regard to the dollar limitation or termination of such section.[36] For purposes of this provision, a production is considered placed in service at the time of initial release, broadcast, or live staged performance (*i.e.*, at the time of the first commercial exhibition, broadcast, or live staged performance of a production to an audience).[37] **E. Exception for certain businesses Not Subject to Interest Limitation.** The provision excludes from the definition of qualified property any property which is primarily used in the trade or business of the furnishing or sale of (1) electrical energy, water, or sewage disposal services, (2) gas or steam through a local distribution system, or (3) transportation of gas or		§ 168(k)

B.1. – BONUS DEPRECIATION

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
<u>Election to accelerate AMT credits in lieu of bonus depreciation</u> A corporation otherwise eligible for additional first-year depreciation may elect to claim additional AMT credits in lieu of claiming additional depreciation with respect to qualified property. In the case of a corporation making this election, the straight line method is used for the regular tax and the AMT with respect to qualified property. A corporation making an election increases the tax liability limitation under section 53(c) on the use of minimum tax credits by the bonus depreciation amount. The aggregate increase in credits allowable by reason of the increased limitation is treated as refundable. The bonus depreciation amount generally is equal to 20 percent of bonus depreciation for qualified property that could be claimed as a deduction absent an election under this provision. As originally enacted, the bonus depreciation amount for all taxable years was limited to the lesser of (1) $30 million or (2) six percent of the minimum tax credits allocable to the adjusted net minimum tax imposed for taxable years beginning before January 1, 2006. However, extensions of this provision have provided that this limitation applies separately to property subject to each extension. For taxable years ending after December 31, 2015, the bonus depreciation amount for a taxable year (as defined under present law with respect to all qualified property) is limited to the lesser of (1) 50 percent of the minimum tax credit for the first taxable year ending after December 31, 2015 (determined before the application of any tax liability limitation) or (2) the minimum tax credit for the taxable year	steam by pipeline, if the rates for such furnishing or sale, as the case may be, have been established or approved by a State or political subdivision thereof, by any agency or instrumentality of the United States, by a public service or public utility commission or other similar body of any State or political subdivision thereof, or by the governing or ratemaking body of an electric cooperative.[38] In addition, the provision excludes from the definition of qualified property any property used in a trade or business that has had floor plan financing indebtedness, if the floor plan financing interest related to such indebtedness was taken into account under the provision allowing a deduction for business interest.[39]		§ 168(k)

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Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
allocable to the adjusted net minimum tax imposed for taxable years ending before January 1, 2016 (determined before the application of any tax liability limitation and determined on a first-in, first-out basis). All corporations treated as a single employer under section 52(a) are treated as one taxpayer for purposes of the limitation, as well as for electing the application of this provision. In the case of a corporation making an election which is a partner in a partnership, for purposes of determining the electing partner's distributive share of partnership items, bonus depreciation does not apply to any qualified property and the straight line method is used with respect to that property. In the case of a partnership having a single corporate partner owning (directly or indirectly) more than 50 percent of the capital and profits interests in the partnership, each partner takes into account its distributive share of partnership depreciation in determining its bonus depreciation amount. **Special rules** **Passenger automobiles** The limitation under section 280F on the amount of depreciation deductions allowed with respect to certain passenger automobiles is increased in the first year by $8,000 for automobiles that qualify (and for which the taxpayer does not elect out of the additional first-year deduction). The $8,000 amount is phased down from $8,000 by $1,600 per calendar year beginning in 2018. Thus, the section 280F increase amount for property placed in service during 2018 is $6,400, and during 2019 is $4,800. While the underlying section 280F limitation is indexed for inflation, the section 280F increase amount is not indexed for inflation. The increase does not apply to a taxpayer who elects to accelerate AMT credits in lieu of bonus depreciation for a taxable year.	1 *See* I.R.C. § 168(k). 2 I.R.C. § 168(k)(6)(A)(i). 3 I.R.C. § 168(k)(6)(B)(i). 4 I.R.C. § 168(k)(6)(C)(i). 5 I.R.C. § 168(k)(2)(F)(iii). 6 In the case of specified plants, this is the year of planting or grafting. 7 I.R.C. § 163(k)(8)(A)(i). 8 I.R.C. § 163(k)(8)(A)(i) 9 I.R.C. § 163(k)(8)(B)(i). 10 I.R.C. § 163(k)(8)(A)(ii) 11 I.R.C. § 168(k)(8)(C)(i). 12 I.R.C. § 168(k)(8)(B)(ii). 13 I.R.C. § 168(k)(8)(D)(i). 14 I.R.C. § 163(k)(8)(C)(ii). 15 I.R.C. § 168(k)(8)(D)(i). 16 I.R.C. § 168(k)(8)(D)(ii). 17 I.R.C. § 168(k)(6)(A)(i); I.R.C. § 168(k)(6)(C)(i). 18 I.R.C. § 168(k)(6)(B)(i). 19 I.R.C. § 168(k)(6)(A)(ii); I.R.C. § 168(k)(6)(C)(ii). 20 I.R.C. § 168(k)(6)(B)(i). 21 I.R.C. § 168(k)(6)(A)(iii); I.R.C. § 168(k)(6)(C)(iii). 22 I.R.C. § 168(k)(6)(B)(ii). 23 I.R.C. § 168(k)(6)(A)(iv); I.R.C. § 168(k)(6)(C)(iv). 24 I.R.C. § 168(k)(6)(B)(iii). 25 I.R.C. § 168(k)(6)(A)(v); I.R.C. § 168(k)(6)(C)(v). 26 I.R.C. § 168(k)(6)(B)(iv). 27 I.R.C. § 168(k)(6)(B)(v). 28 I.R.C. § 168(k)(2)(A)(ii). 29 I.R.C. § 168(k)(2)(E)(ii).		§ 168(k)

B.1. – BONUS DEPRECIATION

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Certain plants bearing fruits and nuts A special election is provided for certain plants bearing fruits and nuts. Under the election, the applicable percentage of the adjusted basis of a specified plant which is planted or grafted after December 31, 2015, and before January 1, 2020, is deductible for regular tax and AMT purposes in the year planted or grafted by the taxpayer, and the adjusted basis is reduced by the amount of the deduction. The percentage is 50 percent for 2017, 40 percent for 2018, and 30 percent for 2019. A specified plant is any tree or vine that bears fruits or nuts, and any other plant that will have more than one yield of fruits or nuts and generally has a preproductive period of more than two years from planting or grafting to the time it begins bearing fruits or nuts. The election is revocable only with the consent of the Secretary, and if the election is made with respect to any specified plant, such plant is not treated as qualified property eligible for bonus depreciation in the subsequent taxable year in which it is placed in service. **Long-term contracts** In general, in the case of a long-term contract, the taxable income from the contract is determined under the percentage-of-completion method. Solely for purposes of determining the percentage of completion under section 460(b)(1)(A), the cost of qualified property with a MACRS recovery period of seven years or less is taken into account as a cost allocated to the contract as if bonus depreciation had not been enacted for property placed in service before January 1, 2020 (January 1, 2021, in the case of longer production period property).	[30] I.R.C. § 168(k)(2)(E)(II); I.R.C. § 179(d)(2)(C); *see also* Treas. Reg. Sec. 1.179-4(c)(1)(iv). [31] I.R.C. § 168(k)(2)(E)(II); I.R.C. § 179(d)(3); *see also* Treas. Reg. Sec. 1.179-4(d). [32] I.R.C. § 168(k)(2)(E)(II); I.R.C. § 179(d)(2)(A); I.R.C. § 179(d)(2)(B); Treas. Reg. Sec. 1.179-4(c). [33] House Report. [34] Act Sec. 2001. [35] I.R.C. § 168(k)(10). [36] I.R.C. § 168(k)(2)(A)(i)(IV); I.R.C. § 168(k)(2)(A)(i)(V). [37] I.R.C. § 168(k)(2)(H); House Report. [38] I.R.C. § 168(k)(9)(A). [39] I.R.C. § 168(k)(9)(B). [40] Act Sec. 13201(h)(1). [41] Act Sec. 13201(h)(2). [42] Act Sec. 13201(h)(1)(B). [43] Act Sec. 3302.		§ 168(k)

B.1. – BONUS DEPRECIATION

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Intangible property MACRS does not apply to certain property, including any motion picture film, video tape, or sound recording, or to any other property if the taxpayer elects to exclude such property from MACRS and the taxpayer properly applies a unit-of-production method or other method of depreciation not expressed in a term of years. Section 197 (amortization of goodwill and certain other intangibles) does not apply to certain intangible property, including certain property produced by the taxpayer or any interest in a film, sound recording, video tape, book or similar property not acquired in a transaction (or a series of related transactions) involving the acquisition of assets constituting a trade or business or substantial portion thereof. Thus, the recovery of the cost of a film, video tape, or similar property that is produced by the taxpayer or is acquired on a “stand-alone” basis by the taxpayer may not be determined under either the MACRS depreciation provisions or under the section 197 amortization provisions. The cost recovery of such property may be determined under section 167, which allows a depreciation deduction for the reasonable allowance for the exhaustion, wear and tear, or obsolescence of the property if it is used in a trade or business or held for the production of income. In addition, the costs of motion picture films, video tapes, sound recordings, copyrights, books, and patents are eligible to be recovered using the income forecast method of depreciation. Expensing of certain qualified film, television and live theatrical productions Under section 181, a taxpayer may elect to deduct the cost of any qualifying film, television and live theatrical production, commencing prior to January 1, 2017, in			§ 168(k)

B.1. – BONUS DEPRECIATION

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
the year the expenditure is incurred in lieu of capitalizing the cost and recovering it through depreciation allowances. A taxpayer may elect to deduct up to $15 million of the aggregate cost of the film or television production under this section. The threshold is increased to $20 million if a significant amount of the production expenditures are incurred in areas eligible for designation as a low-income community or eligible for designation by the Delta Regional Authority as a distressed county or isolated area of distress. A qualified film, television or live theatrical production means any production of a motion picture (whether released theatrically or directly to video cassette or any other format), television program or live staged play if at least 75 percent of the total compensation expended on the production is for services performed in the United States by actors, directors, producers, and other relevant production personnel. The term “compensation” does not include participations and residuals (as defined in section 167(g)(7)(B)). Each episode of a television series is treated as a separate production, and only the first 44 episodes of a particular series qualify under the provision. Qualified productions do not include sexually explicit productions as referenced by section 2257 of title 18 of the U.S. Code. A qualified live theatrical production is defined as a live staged production of a play (with or without music) which is derived from a written book or script and is produced or presented by a commercial entity in any venue which has an audience capacity of not more than 3,000, or a series of venues the majority of which have an audience capacity of not more than			§ 168(k)

B.1. – BONUS DEPRECIATION

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
3,000. In addition, qualified live theatrical productions include any live staged production which is produced or presented by a taxable entity no more than 10 weeks annually in any venue which has an audience capacity of not more than 6,500. In general, in the case of multiple live-staged productions, each such live-staged production is treated as a separate production. Similar to the exclusion for sexually explicit productions from the definition of qualified film or television productions, qualified live theatrical productions do not include stage performances that would be excluded by section 2257(h)(1) of title 18 of the U.S. Code, if such provision were extended to live stage performances. For purposes of recapture under section 1245, any deduction allowed under section 181 is treated as if it were a deduction allowable for amortization.			§ 168(k)

B.2. - MODIFICATIONS TO DEPRECIATION LIMITATIONS ON LUXURY AUTOMOBILES AND PERSONAL USE PROPERTY

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Section 280F(a) limits the annual cost recovery deduction with respect to certain passenger automobiles. This limitation is commonly referred to as the "luxury automobile depreciation limitation." For passenger automobiles placed in service in 2017, and for which the additional first-year depreciation deduction under section 168(k) is not claimed, the maximum amount of allowable depreciation is $3,160 for the year in which the vehicle is placed in service, $5,100 for the second year, $3,050 for the third year, and $1,875 for the fourth and later years in the recovery period. This limitation is indexed for inflation and applies to the aggregate deduction provided under present law for depreciation and section 179 expensing. Hence, passenger automobiles subject to section 280F are eligible for section 179 expensing only to the extent of the applicable limits contained in section 280F. For passenger automobiles eligible for the additional first-year depreciation allowance in 2017, the first-year limitation is increased by an additional $8,000. For purposes of the depreciation limitation, passenger automobiles are defined broadly to include any four-wheeled vehicles that are manufactured primarily for use on public streets, roads, and highways and which are rated at 6,000 pounds unloaded gross vehicle weight or less. In the case of a truck or a van, the depreciation limitation applies to vehicles that are rated at 6,000 pounds gross vehicle weight or less. Sport utility vehicles are treated as a truck for the purpose of applying the section 280F limitation.	The provision increases the depreciation limitations under section 280F that apply to listed property.[1] For passenger automobiles placed in service after December 31, 2017,[2] and for which the additional first-year depreciation deduction under section 168(k) is not claimed, the maximum amount of allowable depreciation is $10,000 for the year in which the vehicle is placed in service,[3] $16,000 for the second year,[4] $9,600 for the third year,[5] and $5,760 for the fourth and later years in the recovery period.[6] The limitations are indexed for inflation for passenger automobiles placed in service after 2018.[7] The provision removes computer or peripheral equipment from the definition of "listed property".[8] Such property is therefore not subject to the heightened substantiation requirements that apply to listed property.[9]	The provision is effective for property placed in service after December 31, 2017, in taxable years ending after such date.[10]	§ 280(f)

[1] See I.R.C. § 280F(1)(A).

[2] Tax Cuts and Jobs Act § 13202(c) (stating the effective date of the statute).

[3] I.R.C. § 280F(a)(1)(A)(i).

[4] I.R.C. § 280F(a)(1)(A)(ii).

[5] I.R.C. § 280F(a)(1)(A)(iii).

[6] I.R.C. § 280F(a)(1)(A)(iv);

[7] I.R.C. § 280F(d)(7).

[8] *See* I.R.C. § 280F(d)(4)(A).

[9] *See* I.R.C. § 274(d).

[10] Tax Cuts and Jobs Act § 13202(c).

B.2. - MODIFICATIONS TO DEPRECIATION LIMITATIONS ON LUXURY AUTOMOBILES AND PERSONAL USE PROPERTY

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Basis not recovered in the recovery period of a passenger automobile is allowable as an expense in subsequent taxable years. The expensed amount is limited in each such subsequent taxable year to the amount of the limitation in the fourth year in the recovery period. **Listed property** In the case of certain listed property, special rules apply. Listed property generally is defined as (1) any passenger automobile; (2) any other property used as a means of transportation; (3) any property of a type generally used for purposes of entertainment, recreation, or amusement; (4) any computer or peripheral equipment; and (5) any other property of a type specified in Treasury regulations. First, if for the taxable year in which the property is placed in service, the use of the property for trade or business purposes does not exceed 50 percent of the total use of the property, then the depreciation deduction with respect to such property is determined under the alternative depreciation system. The alternative depreciation system generally requires the use of the straight-line method and a recovery period equal to the class life of the property. Second, if an individual owns or leases listed property that is used by the individual in connection with the performance of services as an employee, no depreciation deduction, expensing allowance, or deduction for lease payments is available with respect to such use unless the use of the property is for the convenience of the employer and required as a condition of employment. Both limitations apply for purposes of section 179 expensing.			§ 280(f)

B.2. - MODIFICATIONS TO DEPRECIATION LIMITATIONS ON LUXURY AUTOMOBILES AND PERSONAL USE PROPERTY

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
For listed property, no deduction is allowed unless the taxpayer adequately substantiates the expense and business usage of the property. A taxpayer must substantiate the elements of each expenditure or use of listed property, including (1) the amount (e.g., cost) of each separate expenditure and the amount of business or investment use, based on the appropriate measure (*e.g.*, mileage for automobiles), and the total use of the property for the taxable period, (2) the date of the expenditure or use, and (3) the business purposes for the expenditure or use. The level of substantiation for business or investment use of listed property varies depending on the facts and circumstances. In general, the substantiation must contain sufficient information as to each element of every business or investment use.			§ 280(f)

B.3. – MODIFICATIONS OF TREATMENT OF CERTAIN FARM PROPERTY

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
A taxpayer generally must capitalize the cost of property used in a trade or business or held for the production of income and recover such cost over time through annual deductions for depreciation or amortization. Tangible property generally is depreciated under the modified accelerated cost recovery system ("MACRS"), which determines depreciation for different types of property based on an assigned applicable depreciation method, recovery period, and convention. The applicable recovery period for an asset is determined in part by statute and in part by historic Treasury guidance. The "type of property" of an asset is used to determine the "class life" of the asset, which in turn dictates the applicable recovery period for the asset. The MACRS recovery periods applicable to most tangible personal property range from three to 20 years. The depreciation methods generally applicable to tangible personal property are the 200-percent and 150-percent declining balance methods, switching to the straight line method for the first taxable year where using the straight line method with respect to the adjusted basis as of the beginning of that year yields a larger depreciation allowance. The recovery periods for most real property are 39 years for nonresidential real property and 27.5 years for residential rental property. The straight line depreciation method is required for the aforementioned real property. Property used in a farming business is assigned various recovery periods in the same manner as other business property. For example, depreciable assets used in agriculture activities that are assigned a recovery period of 7 years include machinery and	1. **Shortened Recovery Period.** The provision shortens the recovery period from 7 to 5 years for any machinery or equipment (other than any grain bin, cotton ginning asset, fence, or other land improvement) used in a farming business, the original use of which commences with the taxpayer and is placed in service after December 31, 2017.[1] 2. **Partial Repeal of 150-Percent Declining Balance Method for Farming Businesses.** The provision generally repeals the required use of the 150-percent declining balance method for property used in a farming business (*i.e.*, for 3-, 5-, 7-, and 10-year property).[2] The 150- percent declining balance method will continue to apply to any 15-year or 20-year property used in the farming business to which the straight line method does not apply,[3] or to property for which the taxpayer elects the use of the 150-percent declining balance method.[4] 3. **Definition of "Farming Business."** For these purposes, the term "farming business" means a farming business as defined in section 263A(e)(4).[5] Thus, the term ''farming business'' means a trade or business involving the cultivation of land or the raising or harvesting of any agricultural or horticultural commodity (*e.g.*, the trade or business of operating a nursery or sod farm; the raising or harvesting of trees bearing fruit, nuts, or other crops; the raising of ornamental trees (other than evergreen trees that are more than six years old at the time they are severed from their roots); and the raising, shearing, feeding, caring for, training, and management of animals).[6] A farming business	The provision is effective for property placed in service after December 31, 2017, in taxable years ending after such date.[9]	§ 168

B.3. – MODIFICATIONS OF TREATMENT OF CERTAIN FARM PROPERTY

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
equipment, grain bins, and fences (but no other land improvements), that are used in the production of crops or plants, vines, and trees; livestock; the operation of farm dairies, nurseries, greenhouses, sod farms, mushrooms cellars, cranberry bogs, apiaries, and fur farms; and the performance of agriculture, animal husbandry, and horticultural services. Cotton ginning assets are also assigned a recovery period of 7 years. Any single purpose agricultural or horticultural structure, and any tree or vine bearing fruit or nuts are assigned a recovery period of 10 years. Land improvements such as drainage facilities, paved lots, and water wells are assigned a recovery period of 15 years. A 5-year recovery period was assigned to new farm machinery or equipment (other than any grain bin, cotton ginning asset, fence, or other land improvement) which was used in a farming business, the original use of which commenced with the taxpayer after December 31, 2008, and which was placed in service before January 1, 2010. Any property (other than nonresidential real property, residential rental property, and trees or vines bearing fruits or nuts) used in a farming business is subject to the 150- percent declining balance method. Under a special accounting rule, certain taxpayers engaged in the business of farming who elect to deduct preproductive period expenditures are required to depreciate all farming assets using the alternative depreciation system (*i.e.*, using longer recovery periods and the straight line method).	includes processing activities that are normally incident to the growing, raising, or harvesting of agricultural or horticultural products.[7] A farming business does not include contract harvesting of an agricultural or horticultural commodity grown or raised by another taxpayer, or merely buying and reselling plants or animals grown or raised by another taxpayer.[8] [1] I.R.C. § 168(e)(3)(B)(vii). [2] *See* I.R.C. § 168(b)(2). [3] I.R.C. § 168(b)(2)(A). [4] I.R.C. § 168(b)(2), (5). [5] I.R.C. § 168(e)(3)(B)(vii). [6] Treas. Reg. § 1.263A–4(a)(4)(i). [7] Treas. Reg. § 1.263A–4(a)(4)(ii). [8] Treas. Reg. § 1.263A–4(a)(4)(i). [9] Tax Cuts and Jobs Act § 13202(c).		§ 168

B.4. - APPLICABLE RECOVERY PERIOD FOR REAL PROPERTY

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
A taxpayer generally must capitalize the cost of property used in a trade or business or held for the production of income and recover such cost over time through annual deductions for depreciation or amortization. Tangible property generally is depreciated under the modified accelerated cost recovery system ("MACRS"), which determines depreciation for different types of property based on an assigned applicable depreciation method, recovery period, and convention. **<u>Recovery periods and depreciation methods</u>** The applicable recovery period for an asset is determined in part by statute and in part by historic Treasury guidance. The "type of property" of an asset is used to determine the "class life" of the asset, which in turn dictates the applicable recovery period for the asset. The MACRS recovery periods applicable to most tangible personal property range from three to 20 years. The depreciation methods generally applicable to tangible personal property are the 200-percent and 150-percent declining balance methods, switching to the straight line method for the first taxable year where using the straight line method with respect to the adjusted basis as of the beginning of that year yields a larger depreciation allowance. The recovery periods for most real property are 39 years for nonresidential real property and 27.5 years for residential rental property. The straight line depreciation method is required for the aforementioned real property.	1. **Qualified Improvement Property.** The Act eliminates the separate definitions of qualified leasehold improvement, qualified restaurant, and qualified retail improvement property, and provides a new category for qualified improvement property.[1] While the Conference Report indicates that qualified improvement property will have a 15-year recovery period, the statute does not reflect the change. Presumably, the omission will be corrected as part of technical corrections. The term "qualified improvement property" means any improvement to an interior portion of a building which is nonresidential real property if such improvement is placed in service after the date such building was first placed in service.[2] Such term shall not include any improvement for which the expenditure is attributable to (a) the enlargement of the building;[3] (b) any elevator or escalator;[4] (c) the internal structural framework of the building.[5] 2. **Conforming Amendment to Election to Expense Certain Depreciable Assets.** As a conforming amendment, the provision replaces the references in section 179(f) (relating to the election to expense certain depreciable assets) to qualified leasehold improvement property, qualified restaurant property, and qualified retail improvement property with a reference to qualified improvement property. Thus, for example, the provision allows section 179 expensing for improvement property without regard to whether the improvements are property subject to a lease, placed in service more than three years after the date the building was first placed in service, or made to a restaurant building.[6]	The provision is effective for property placed in service after December 31, 2017.[8]	§ 168

B.4. - APPLICABLE RECOVERY PERIOD FOR REAL PROPERTY

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Placed-in-service conventions Depreciation of an asset begins when the asset is deemed to be placed in service under the applicable convention. Under MACRS, nonresidential real property, residential rental property, and any railroad grading or tunnel bore generally are subject to the mid-month convention, which treats all property placed in service during any month (or disposed of during any month) as placed in service (or disposed of) on the mid-point of such month. All other property generally is subject to the half-year convention, which treats all property placed in service during any taxable year (or disposed of during any taxable year) as placed in service (or disposed of) on the mid-point of such taxable year to reflect the assumption that assets are placed in service ratably throughout the year. However, if substantial property is placed in service during the last three months of a taxable year, a special rule requires use of the mid-quarter convention, designed to prevent the recognition of disproportionately large amounts of first- year depreciation under the half-year convention. **Depreciation of additions or improvements to property** The recovery period for any addition or improvement to real or personal property begins on the later of (1) the date on which the addition or improvement is placed in service, or (2) the date on which the property with respect to which such addition or improvement is made is placed in service. Any MACRS deduction for an addition or improvement to any property is to be computed in the same manner as the deduction for the underlying property would be if such property were placed in service at the same time as such addition or	Restaurant building property placed in service after December 31, 2017, that does not meet the definition of qualified improvement property is not eligible for section 179 expensing.[7] [1] I.R.C. § 168(b)(3)(G). [2] I.R.C. § 168(e)(6)(A). [3] I.R.C. § 168(e)(6)(B)(i) [4] I.R.C. § 168(e)(6)(B)(ii). [5] I.R.C. § 168(e)(6)(B)(iii). [6] Conf. Report. [7] Conf. Report. [8] Act Sec. 13204(b)(1).		§ 168

B.4. - APPLICABLE RECOVERY PERIOD FOR REAL PROPERTY

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
improvement. Thus, for example, the cost of an improvement to a building that constitutes nonresidential real property is recovered over 39 years using the straight line method and mid-month convention. Certain improvements to nonresidential real property are eligible for the additional first-year depreciation deduction if the other requirements of section 168(k) are met (*i.e.*, improvements that constitute "qualified improvement property"). **<u>Qualified leasehold improvement property</u>** Section 168(e)(3)(E)(iv) provides a statutory 15-year recovery period for qualified leasehold improvement property. Qualified leasehold improvement property is any improvement to an interior portion of a building that is nonresidential real property, provided certain requirements are met. The improvement must be made under or pursuant to a lease either by the lessee (or sublessee), or by the lessor, of that portion of the building to be occupied exclusively by the lessee (or sublessee). The improvement must be placed in service more than three years after the date the building was first placed in service. Qualified leasehold improvement property does not include any improvement for which the expenditure is attributable to the enlargement of the building, any elevator or escalator, any structural component benefiting a common area, or the internal structural framework of the building. If a lessor makes an improvement that qualifies as qualified leasehold improvement property, such improvement does not qualify as qualified leasehold improvement property to any subsequent owner of such improvement. An exception to the rule applies in the case of death and certain transfers of property that qualify for non-recognition treatment.			§ 168

B.4. - APPLICABLE RECOVERY PERIOD FOR REAL PROPERTY

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Qualified leasehold improvement property is generally recovered using the straight-line method and a half-year convention, and is eligible for the additional first-year depreciation deduction if the other requirements of section 168(k) are met. **<u>Qualified restaurant property</u>** Section 168(e)(3)(E)(v) provides a statutory 15-year recovery period for qualified restaurant property. Qualified restaurant property is any section 1250 property that is a building or an improvement to a building, if more than 50 percent of the building's square footage is devoted to the preparation of, and seating for on-premises consumption of, prepared meals. Qualified restaurant property is recovered using the straight-line method and a half-year convention. Additionally, qualified restaurant property is not eligible for the additional first- year depreciation deduction unless it also satisfies the definition of qualified improvement property. Retail establishments that qualify for the 15-year recovery period include those primarily engaged in the sale of goods. Examples of these retail establishments include, but are not limited to, grocery stores, clothing stores, hardware stores, and convenience stores. Establishments primarily engaged in providing services, such as professional services, financial services, personal services, health services, and entertainment, do not qualify. Generally, it is intended that businesses defined as a store retailer under the current North American Industry Classification System (industry sub-sectors 441 through 453) qualify while those in other industry classes do not qualify.			§ 168

B.4. - APPLICABLE RECOVERY PERIOD FOR REAL PROPERTY

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Qualified retail improvement property is recovered using the straight-line method and a half-year convention, and is eligible for the additional first-year depreciation deduction if the other requirements of section 168(k) are met. **<u>Alternative depreciation system</u>** The alternative depreciation system ("ADS") is required to be used for tangible property used predominantly outside the United States, certain tax-exempt use property, tax-exempt bond financed property, and certain imported property covered by an Executive order. An election to use ADS is available to taxpayers for any class of property for any taxable year. Under ADS, all property is depreciated using the straight line method over recovery periods which generally are equal to the class life of the property, with certain exceptions. For example nonresidential real and residential rental property have a 40-year ADS recovery period, while qualified leasehold improvement property, qualified restaurant property, and qualified retail improvement property have a 39-year ADS recovery period.			§ 168

B.5. – USE OF ALTERNATIVE DEPRECIATION SYSTEM FOR ELECTING FARMING BUSINESSES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
A taxpayer generally must capitalize the cost of property used in a trade or business or held for the production of income and recover such cost over time through annual deductions for depreciation or amortization. Tangible property generally is depreciated under the modified accelerated cost recovery system ("MACRS"), which determines depreciation for different types of property based on an assigned applicable depreciation method, recovery period, and convention. The applicable recovery period for an asset is determined in part by statute and in part by historic Treasury guidance. The "type of property" of an asset is used to determine the "class life" of the asset, which in turn dictates the applicable recovery period for the asset. The MACRS recovery periods applicable to most tangible personal property range from three to 20 years. The depreciation methods generally applicable to tangible personal property are the 200-percent and 150-percent declining balance methods, switching to the straight line method for the first taxable year where using the straight line method with respect to the adjusted basis as of the beginning of that year yields a larger depreciation allowance. The recovery periods for most real property are 39 years for nonresidential real property and 27.5 years for residential rental property. The straight line depreciation method is required for the aforementioned real property. Property used in a farming business is assigned various recovery periods in the same manner as other business property. For example, depreciable assets used in agriculture activities that are assigned a recovery period of 7 years include machinery and	The provision requires an electing farming business, *i.e.*, a farming business[1] electing out of the limitation on the deduction for interest,[2] to use the Alternative Depreciation System to depreciate any property with a recovery period of 10 years or more (*e.g.*, property such as single purpose agricultural or horticultural structures, trees or vines bearing fruit or nuts, farm buildings, and certain land improvements[3]).[4] [1] *See* I.R.C. § 263A(4). [2] I.R.C. § 163(j)(7)(C) [3] I.R.C. § 168(e)(3)(D). [4] I.R.C. § 168(g)(1)(G). [5] Tax Cuts and Jobs Act § 13205(b).	The provision is effective for taxable years beginning after December 31, 2017.[5]	§ 168

B.5 – USE OF ALTERNATIVE DEPRECIATION SYSTEM FOR ELECTING FARMING BUSINESSES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
equipment, grain bins, and fences (but no other land improvements), that are used in the production of crops or plants, vines, and trees; livestock; the operation of farm dairies, nurseries, greenhouses, sod farms, mushrooms cellars, cranberry bogs, apiaries, and fur farms; and the performance of agriculture, animal husbandry, and horticultural services. Cotton ginning assets are also assigned a recovery period of 7 years. Any single purpose agricultural or horticultural structure, and any tree or vine bearing fruit or nuts are assigned a recovery period of 10 years. Land improvements such as drainage facilities, paved lots, and water wells are assigned a recovery period of 15 years. A 5-year recovery period was assigned to new farm machinery or equipment (other than any grain bin, cotton ginning asset, fence, or other land improvement) which was used in a farming business, the original use of which commenced with the taxpayer after December 31, 2008, and which was placed in service before January 1, 2010. Any property (other than nonresidential real property, residential rental property, and trees or vines bearing fruits or nuts) used in a farming business is subject to the 150- percent declining balance method. **Alternative depreciation system** The alternative depreciation system ("ADS") is required to be used for tangible property used predominantly outside the United States, certain tax-exempt use property, tax-exempt bond financed property, and certain imported property covered by an Executive order. An election to use ADS is available to taxpayers for any class of property for any taxable year. Under ADS, all property is			§ 168

B.5 – USE OF ALTERNATIVE DEPRECIATION SYSTEM FOR ELECTING FARMING BUSINESSES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
depreciated using the straight line method over recovery periods which generally are equal to the class life of the property, with certain exceptions. For example, any single purpose agricultural or horticultural structure has a 15-year ADS recovery period, while any tree or vine bearing fruit or nuts has a 20-year ADS recovery period. Similarly, land improvements such as drainage facilities, paved lots, and water wells have an ADS recovery period of 20 years. Under a special accounting rule, certain taxpayers engaged in the business of farming who elect to deduct preproductive period expenditures under the uniform capitalization rules are required to depreciate all farming assets using ADS.			§ 168

Tax Reform
Section C

C.1. - EXPANSION OF § 179 EXPENSING

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
A taxpayer generally must capitalize the cost of property used in a trade or business or held for the production of income and recover such cost over time through annual deductions for depreciation or amortization. Tangible property generally is depreciated under the modified accelerated cost recovery system ("MACRS"), which determines depreciation for different types of property based on an assigned applicable depreciation method, recovery period, and convention. **<u>Election to expense certain depreciable business assets</u>** A taxpayer may elect under section 179 to deduct (or "expense") the cost of qualifying property, rather than to recover such costs through depreciation deductions, subject to limitation. The maximum amount a taxpayer may expense is $500,000 of the cost of qualifying property placed in service for the taxable year. The $500,000 amount is reduced (but not below zero) by the amount by which the cost of qualifying property placed in service during the taxable year exceeds $2,000,000. The $500,000 and $2,000,000 amounts are indexed for inflation for taxable years beginning after 2015. In general, qualifying property is defined as depreciable tangible personal property that is purchased for use in the active conduct of a trade or business. Qualifying property also includes off-the-shelf computer software and qualified real property (i.e., qualified leasehold improvement property, qualified restaurant property, and qualified retail improvement property). Qualifying property excludes any property described in section 50(b) (*i.e.*, certain property not eligible for the investment tax credit).	**1. Increasing the Expensing Ceiling and Phase-out Threshold.** The provision increases the maximum amount a taxpayer may expense under section 179 to $1,000,000, and increases the phase-out threshold amount to $2,500,000.[1] Thus, the provision provides that the maximum amount a taxpayer may expense, for taxable years beginning after 2017, is $1,000,000 of the cost of qualifying property placed in service for the taxable year.[2] The $1,000,000 amount is reduced (but not below zero) by the amount by which the cost of qualifying property placed in service during the taxable year exceeds $2,500,000.[3] The $1,000,000 and $2,500,000 amounts, as well as the $25,000 sport utility vehicle limitation, are indexed for inflation for taxable years beginning after 2018.[4] **2. Expanded Definition of Section 179 Property.** The provision expands the definition of section 179 property to include certain depreciable tangible personal property used predominantly to furnish lodging or in connection with furnishing lodging.[5] **3. Expanded Definition of Qualified Real Property.** The provision also expands the definition of qualified real property eligible for section 179 expensing to include any of the following improvements to nonresidential real property placed in service after the date such property was first placed in service: roofs; heating, ventilation, and air-conditioning property; fire protection and alarm systems; and security systems.[6]	The provision applies to property placed in service in taxable years beginning after December 31, 2017.[7]	§ 179

C.1. - EXPANSION OF § 179 EXPENSING

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Passenger automobiles subject to the section 280F limitation are eligible for section 179 expensing only to the extent of the dollar limitations in section 280F. For sport utility vehicles above the 6,000 pound weight rating and not more than the 14,000 pound weight rating, which are not subject to the limitation under section 280F, the maximum cost that may be expensed for any taxable year under section 179 is $25,000 (the "sport utility vehicle limitation"). The amount eligible to be expensed for a taxable year may not exceed the taxable income for such taxable year that is derived from the active conduct of a trade or business (determined without regard to this provision). Any amount that is not allowed as a deduction because of the taxable income limitation may be carried forward to succeeding taxable years (subject to limitations). No general business credit under section 38 is allowed with respect to any amount for which a deduction is allowed under section 179. If a corporation makes an election under section 179 to deduct expenditures, the full amount of the deduction does not reduce earnings and profits. Rather, the expenditures that are deducted reduce corporate earnings and profits ratably over a five-year period. An expensing election is made under rules prescribed by the Secretary. In general, any election or specification made with respect to any property may not be revoked except with the consent of the Commissioner. However, an election or specification under section 179 may be revoked by the taxpayer without consent of the Commissioner.	[1] I.R.C. § 179(b)(1), (2). [2] I.R.C. § 179(b)(1). [3] I.R.C. § 179(b)(2). [4] I.R.C. § 179(b)(6). [5] I.R.C. § 179(d)(1) (flush language). [6] I.R.C. § 179(f). [7] Tax Cuts and Jobs Act, § 13101(d).		§ 179

C.2. - SMALL BUSINESS ACCOUNTING METHOD REFORM AND SIMPLIFICATION

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
General rule for methods of accounting Section 446 generally allows a taxpayer to select the method of accounting to be used to compute taxable income, provided that such method clearly reflects the income of the taxpayer. The term "method of accounting" includes not only the overall method of accounting used by the taxpayer, but also the accounting treatment of any one item. Permissible overall methods of accounting include the cash receipts and disbursements method ("cash method"), an accrual method, or any other method (including a hybrid method) permitted under regulations prescribed by the Secretary. Examples of any one item for which an accounting method may be adopted include cost recovery, revenue recognition, and timing of deductions. For each separate trade or business, a taxpayer is entitled to adopt any permissible method, subject to certain restrictions. A taxpayer filing its first return may adopt any permissible method of accounting in computing taxable income for such year. Except as otherwise provided, section 446(e) requires taxpayers to secure consent of the Secretary before changing a method of accounting. The regulations under this section provide rules for determining: (1) what a method of accounting is, (2) how an adoption of a method of accounting occurs, and (3) how a change in method of accounting is effectuated.	1. **Expansion of Taxpayers Eligible to Use Cash Method.** The provision expands the universe of taxpayers that may use the cash method of accounting.[1] Under the provision, the cash method of accounting may be used by taxpayers, other than tax shelters, that satisfy the gross receipts test, regardless of whether the purchase, production, or sale of merchandise is an income-producing factor.[2] **a. Gross Receipts Test.** The gross receipts test is met for a particular tax year if the annual average gross receipts over the three years previous tax years do not exceed $25 million (the "$25 million gross receipts test").[3] The $25 million amount is indexed for inflation for taxable years beginning after 2018.[4] **b. Expansion of Farming C Corporations Eligible to Use Cash Method.** The provision expands the universe of farming C corporations (and farming partnerships with a C corporation partner) that may use the cash method to include any farming C corporation (or farming partnership with a C corporation partner) that meets the $25 million gross receipts test.[5] **c. Retention of Certain Exceptions.** The provision retains the exceptions from the required use of the accrual method for qualified personal service corporations and taxpayers other than C corporations.[6]	The provisions to expand the universe of taxpayers eligible to use the cash method, exempt certain taxpayers from the requirement to keep inventories, and expand the exception from the uniform capitalization rules apply to taxable years beginning after December 31, 2017.[19] The provision to expand the exception for small construction contracts from the requirement to use the percentage-of-completion method applies to contracts entered into after December 31, 2017, in taxable years ending after such date.[20]	§ 263A § 448 § 460 § 471

C.2. - SMALL BUSINESS ACCOUNTING METHOD REFORM AND SIMPLIFICATION

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
<u>Cash and accrual methods</u> Taxpayers using the cash method generally recognize items of income when actually or constructively received and items of expense when paid. The cash method is administratively easy and provides the taxpayer flexibility in the timing of income recognition. It is the method generally used by most individual taxpayers, including farm and nonfarm sole proprietorships. Taxpayers using an accrual method generally accrue items of income when all the events have occurred that fix the right to receive the income and the amount of the income can be determined with reasonable accuracy. Taxpayers using an accrual method of accounting generally may not deduct items of expense prior to when all events have occurred that fix the obligation to pay the liability, the amount of the liability can be determined with reasonable accuracy, and economic performance has occurred. Accrual methods of accounting generally result in a more accurate measure of economic income than does the cash method. The accrual method is often used by businesses for financial accounting purposes. A C corporation, a partnership that has a C corporation as a partner, or a tax-exempt trust or corporation with unrelated business income generally may not use the cash method. Exceptions are made for farming businesses, qualified personal service corporations, and the aforementioned entities to the extent their average annual gross receipts do not exceed $5 million for all prior years (including the prior taxable years of any predecessor of the entity) (the "gross receipts test").	Thus, qualified personal service corporations, partnerships without C corporation partners, S corporations, and other passthrough entities are allowed to use the cash method without regard to whether they meet the $25 million gross receipts test,[7] so long as the use of such method clearly reflects income.[8] **2. Exemption from Inventory Requirement.** In addition, the provision also exempts certain taxpayers from the requirement to keep inventories. Specifically, taxpayers that meet the $25 million gross receipts test are not required to account for inventories under section 471,[9] but rather may use a method of accounting for inventories that either (1) treats inventories as non-incidental materials and supplies,[10] or (2) conforms to the taxpayer's financial accounting treatment of inventories.[11] **3. Expanded UNICAP Exception for Small Taxpayers.** The provision expands the exception for small taxpayers from the uniform capitalization rules. Under the provision, any producer or reseller that meets the $25 million gross receipts test is exempted from the application of section 263A.[12] The provision retains the exemptions from the uniform capitalization rules that are not based on a taxpayer's gross receipts.[13] **4. Expanded Small Construction Contract Exception.** Finally, the provision expands the exception for small construction contracts from the requirement to use the percentage-of-completion method.[14] Under the provision, contracts within this exception are those contracts for the construction or improvement of real property if the contract:		§ 263A § 448 § 460 § 471

C.2. - SMALL BUSINESS ACCOUNTING METHOD REFORM AND SIMPLIFICATION

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
The cash method may not be used by any tax shelter. In addition, the cash method generally may not be used if the purchase, production, or sale of merchandise is an income producing factor. Such taxpayers generally are required to keep inventories and use an accrual method with respect to inventory items. A farming business is defined as a trade or business of farming, including operating a nursery or sod farm, or the raising or harvesting of trees bearing fruit, nuts, or other crops, timber, or ornamental trees. Such farming businesses are not precluded from using the cash method regardless of whether they meet the gross receipts test. However, section 447 generally requires a farming C corporation (and any farming partnership if a corporation is a partner in such partnership) to use an accrual method of accounting. Section 447 does not apply to nursery or sod farms, to the raising or harvesting of trees (other than fruit and nut trees), nor to farming C corporations meeting a gross receipts test with a $1 million threshold. For family farm C corporations, the threshold under the gross receipts test is $25 million. A qualified personal service corporation is a corporation: (1) substantially all of whose activities involve the performance of services in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts, or consulting, and (2) substantially all of the stock of which is owned by current or former employees performing such services, their estates, or heirs. Qualified personal service corporations are allowed to use the cash method without regard to whether they meet the gross receipts test.	(1) is expected (at the time such contract is entered into) to be completed within two years of commencement of the contract and (2) is performed by a taxpayer that (for the taxable year in which the contract was entered into) meets the $25 million gross receipts test.[15] 5. **Failure of $25 Million Gross Receipts Test.** Under the provision, a taxpayer who fails the $25 million gross receipts test would not be eligible for any of the aforementioned exceptions (*i.e.*, from the accrual method, from keeping inventories, from applying the uniform capitalization rules, or from using the percentage-of completion method) for such taxable year.[16] 6. **Change in Taxpayer's Method of Accounting.** Application of the provisions to expand the universe of taxpayers eligible to use the cash method, exempt certain taxpayers from the requirement to keep inventories, and expand the exception from the uniform capitalization rules is a change in the taxpayer's method of accounting for purposes of section 481.[17] Application of the exception for small construction contracts from the requirement to use the percentage-of-completion method is applied on a cutoff basis for all similarly classified contracts (hence there is no adjustment under section 481(a) for contracts entered into before January 1, 2018).[18]		§ 263A § 448 § 460 § 471

C.2. - SMALL BUSINESS ACCOUNTING METHOD REFORM AND SIMPLIFICATION

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Accounting for inventories In general, for Federal income tax purposes, taxpayers must account for inventories if the production, purchase, or sale of merchandise is an income-producing factor to the taxpayer. Treasury regulations also provide that in any case in which the use of inventories is necessary to clearly reflect income, the accrual method must be used with regard to purchases and sales. However, an exception is provided for taxpayers whose average annual gross receipts do not exceed $1 million. A second exception is provided for taxpayers in certain industries whose average annual gross receipts do not exceed $10 million and that are not otherwise prohibited from using the cash method under section 448. Such taxpayers may account for inventory as materials and supplies that are not incidental (*i.e.*, "non-incidental materials and supplies"). In those circumstances in which a taxpayer is required to account for inventory, the taxpayer must maintain inventory records to determine the cost of goods sold during the taxable period. Cost of goods sold generally is determined by adding the taxpayer's inventory at the beginning of the period to the purchases made during the period and subtracting from that sum the taxpayer's inventory at the end of the period. Because of the difficulty of accounting for inventory on an item-by-item basis, taxpayers often use conventions that assume certain item or cost flows. Among these conventions are the first-in, first-out ("FIFO") method, which assumes that the items in ending inventory are those most recently acquired by the taxpayer, and the last-in, first-out ("LIFO") method, which assumes that the items in ending inventory are those earliest acquired by the taxpayer.	The provision to expand the exception for small construction contracts from the requirement to use the percentage-of-completion method applies to contracts entered into after December 31, 2017, in taxable years ending after such date. [1] *See* I.R.C. § 448(b). [2] I.R.C. § 448(b)(3). [3] I.R.C. § 448(c)(1). [4] I.R.C. § 448(c)(4). [5] I.R.C. § 447(c)(2). [6] *See* I.R.C. § 448(a), (b)(2). [7] I.R.C. § 448(a), (b)(2). Consistent with present law, the cash method generally may not be used by taxpayers, other than those that meet the $25 million gross receipts test, if the purchase, production, or sale of merchandise is an income-producing factor. Treas. Reg. § 1.446-1(a)(4)(i), (c)(2). In addition, the cash method may not be used by a tax shelter. I.R.C. § 448(a)(3). [8] I.R.C. § 446(b). [9] I.R.C. § 471(c)(1)(A). In the case of a sole proprietorship, the $25 million gross receipts test is applied as if the sole proprietorship is a corporation or partnership. I.R.C. § 471(c)(3). [10] Consistent with present law, a deduction is generally permitted for the cost of non-incidental materials and supplies in the taxable year in which they are first used or are consumed in the taxpayer's operations. *See* Treas. Reg. § 1.162-3(a)(1).		§ 263A § 448 § 460 § 471

C.2. - SMALL BUSINESS ACCOUNTING METHOD REFORM AND SIMPLIFICATION

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Uniform capitalization The uniform capitalization rules require certain direct and indirect costs allocable to real or tangible personal property produced by the taxpayer to be included in either inventory or capitalized into the basis of such property, as applicable. For real or personal property acquired by the taxpayer for resale, section 263A generally requires certain direct and indirect costs allocable to such property to be included in inventory. Section 263A provides a number of exceptions to the general uniform capitalization requirements. One such exception exists for certain small taxpayers who acquire property for resale and have $10 million or less of average annual gross receipts; such taxpayers are not required to include additional section 263A costs in inventory. Another exception exists for taxpayers who raise, harvest, or grow trees. Under this exception, section 263A does not apply to trees raised, harvested, or grown by the taxpayer (other than trees bearing fruit, nuts, or other crops, or ornamental trees) and any real property underlying such trees. Similarly, the uniform capitalization rules do not apply to any plant having a preproductive period of two years or less or to any animal, which is produced by a taxpayer in a farming business (unless the taxpayer is required to use an accrual method of accounting under section 447 or 448(a)(3)). Freelance authors, photographers, and artists also are exempt from section 263A for any qualified creative expenses. **Accounting for long-term contracts** In general, in the case of a long-term contract, the taxable income from the contract is determined under the percentage-of-completion method.	[11] I.R.C. § 471(c)(1)(B). The taxpayer's financial accounting treatment of inventories is determined by reference to the method of accounting used in the taxpayer's applicable financial statement, or, if the taxpayer does not have an applicable financial statement, the method of accounting used in the taxpayer's book and records prepared in accordance with the taxpayer's accounting procedures. [12] I.R.C. § 263A(i)(1). In the case of a sole proprietorship, the $25 million gross receipts test is applied as if the sole proprietorship is a corporation or partnership. I.R.C. § 263A(i)(2). [13] *See* I.R.C. § 263(h). [14] I.R.C. § 460(e)(1). [15] *Id*. In the case of a sole proprietorship, the $25 million gross receipts test is applied as if the sole proprietorship is a corporation or partnership. I.R.C. § 460(e)(2)(A). [16] *See* I.R.C. §§ 448(b)(3), 471(c)(1)(A), 263A(i)(1), 460(e)(1)(ii). [17] I.R.C. §§ 448(c)(7); 471(c)(4); 263A(i)(3). [18] I.R.C. § 460(e)(2)(B). [19] Tax Cuts and Jobs Acts, § 13012(e)(1). [20] Tax Cuts and Jobs Acts, § 13012(e)(3).		§ 263A § 448 § 460 § 471

C.2. - SMALL BUSINESS ACCOUNTING METHOD REFORM AND SIMPLIFICATION

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Under this method, the taxpayer must include in gross income for the taxable year an amount equal to the product of (1) the gross contract price and (2) the percentage of the contract completed during the taxable year. The percentage of the contract completed during the taxable year is determined by comparing costs allocated to the contract and incurred before the end of the taxable year with the estimated total contract costs. Costs allocated to the contract typically include all costs (including depreciation) that directly benefit or are incurred by reason of the taxpayer's long-term contract activities. The allocation of costs to a contract is made in accordance with regulations. Costs incurred with respect to the long-term contract are deductible in the year incurred, subject to general accrual method of accounting principles and limitations. An exception from the requirement to use the percentage-of-completion method is provided for certain construction contracts ("small construction contracts"). Contracts within this exception are those contracts for the construction or improvement of real property if the contract: (1) is expected (at the time such contract is entered into) to be completed within two years of commencement of the contract and (2) is performed by a taxpayer whose average annual gross receipts for the prior three taxable years do not exceed $10 million. Thus, long-term contract income from small construction contracts must be reported consistently using the taxpayer's exempt contract method. Permissible exempt contract methods include the completed contract method, the exempt-contract percentage-of-completion method, the percentage-of-completion method, or any other permissible method.			§ 263A § 448 § 460 § 471

C.3. - MODIFICATION OF TREATMENT OF S CORPORATION CONVERSIONS TO C CORPORATIONS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Changes in accounting method **Cash and accrual methods in general** Taxpayers using the cash method generally recognize items of income when actually or constructively received and items of expense when paid. The cash method is administratively easy and provides the taxpayer flexibility in the timing of income recognition. It is the method generally used by most individual taxpayers, including farm and nonfarm sole proprietorships. Taxpayers using an accrual method generally accrue items of income when all the events have occurred that fix the right to receive the income and the amount of the income can be determined with reasonable accuracy. Taxpayers using an accrual method of accounting generally may not deduct items of expense prior to when all events have occurred that fix the obligation to pay the liability, the amount of the liability can be determined with reasonable accuracy, and economic performance has occurred. Accrual methods of accounting generally result in a more accurate measure of economic income than does the cash method. The accrual method is often used by businesses for financial accounting purposes. A C corporation, a partnership that has a C corporation as a partner, or a tax-exempt trust or corporation with unrelated business income generally may not use the cash method. Exceptions are made for farming businesses, qualified personal service corporations, and the aforementioned entities to the extent their average annual gross receipts do not exceed $5 million for all prior years (including the prior taxable years of any predecessor of the entity) (the "gross receipts test").	1. **Adjustments Attributable to Conversion from S Corporation to C Corporation.** Under the provision, any section 481(a) adjustment of an eligible terminated S corporation attributable to the revocation of its S corporation election (*i.e.*, a change from the cash method to an accrual method) is taken into account ratably during the six-taxable-year period beginning with the year of change.[1] 2. **Eligible Terminated S Corporation.** An eligible terminated S corporation is any C corporation which (1) was an S corporation the day before the enactment of the Tax Cuts and Jobs Act, (2) revokes its S corporation election under section 1362(a) within two years after the date of such enactment, and (3) all of the owners of which on the date the S corporation election is revoked are the same owners (and in identical proportions) as the owners on the date of such enactment.[2] 3. **Cash Distributions After S-Corp Revocation.** Under the provision, in the case of certain distributions of money by an eligible terminated S corporation, the accumulated adjustments account[3] shall be allocated to such distribution, and the distribution shall be chargeable to accumulated earnings and profits, in the same ratio as the amount of the accumulated adjustments account bears to the amount the accumulated earnings and profits.[4]	The provision is effective upon enactment.	§ 481 § 1371

C.3. - MODIFICATION OF TREATMENT OF S CORPORATION CONVERSIONS TO C CORPORATIONS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
The cash method may not be used by any tax shelter. In addition, the cash method generally may not be used if the purchase, production, or sale of merchandise is an income producing factor. Such taxpayers generally are required to keep inventories and use an accrual method with respect to inventory items. **<u>Procedures for changing a method of accounting</u>** A taxpayer filing its first return may adopt any permissible method of accounting in computing taxable income for such year. Except as otherwise provided, section 446(e) requires taxpayers to secure consent of the Secretary before changing a method of accounting. The regulations under this section provide rules for determining: (1) what a method of accounting is, (2) how an adoption of a method of accounting occurs, and (3) how a change in method of accounting is effectuated. Section 481 prescribes the rules to be followed in computing taxable income in cases where the taxable income of the taxpayer is computed under a different method than the prior year (*e.g.*, when changing from the cash method to an accrual method). In computing taxable income for the year of change, the taxpayer must take into account those adjustments which are determined to be necessary solely by reason of such change in order to prevent items of income or expense from being duplicated or omitted. The year of change is the taxable year for which the taxable income of the taxpayer is computed under a different method than the prior year. Congress has provided the Secretary with the authority to prescribe the timing and manner in which such adjustments are taken into account in computing taxable income.	[1] I.R.C. § 481(d)(1). [2] I R.C. § 481(d)(2). [3] I.R.C. § 1368(e)(1). [4] I.R.C. § 1371(f).		§ 481 § 1371

C.3. - MODIFICATION OF TREATMENT OF S CORPORATION CONVERSIONS TO C CORPORATIONS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Net adjustments that decrease taxable income generally are taken into account entirely in the year of change, and net adjustments that increase taxable income generally are taken into account ratably during the four-taxable-year period beginning with the year of change. **<u>Post-termination distributions</u>** Under present law, in the case of an S corporation that converts to a C corporation, distributions of cash by the C corporation to its shareholders during the post-termination transition period (to the extent of the amount in the accumulated adjustment account) are tax-free to the shareholders and reduce the adjusted basis of the stock. The post-termination transition period is generally the one-year period after the S corporation election terminates.			§ 481 § 1371

Tax Reform
Section D

D.1. – LIMITATION ON BUSINESS INTEREST

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Interest deduction Interest paid or accrued by a business generally is deductible in the computation of taxable income subject to a number of limitations. Interest is generally deducted by a taxpayer as it is paid or accrued, depending on the taxpayer's method of accounting. For all taxpayers, if an obligation is issued with original issue discount ("OID"), a deduction for interest is allowable over the life of the obligation on a yield to maturity basis. Generally, OID arises where interest on a debt instrument is not calculated based on a qualified rate and required to be paid at least annually. **Investment interest expense** In the case of a taxpayer other than a corporation, the deduction for interest on indebtedness that is allocable to property held for investment ("investment interest") is limited to the taxpayer's net investment income for the taxable year. Disallowed investment interest is carried forward to the next taxable year. Net investment income is investment income net of investment expenses. Investment income generally consists of gross income from property held for investment, and investment expense includes all deductions directly connected with the production of investment income (*e.g.*, deductions for investment management fees) other than deductions for interest. The two-percent floor on miscellaneous itemized deductions allows taxpayers to deduct investment expenses connected with investment income only to the extent such deductions exceed two percent of the taxpayer's adjusted gross income ("AGI").	**1. General Rule.** In the case of any taxpayer for any taxable year, the deduction for business interest is limited to the sum of (1) business interest income;[1] (2) 30 percent of the adjusted taxable income of the taxpayer for the taxable year (but not less than zero);[2] and (3) the floor plan financing interest of the taxpayer for the taxable year.[3] By including business interest income and floor plan financing interest in the limitation, the rule operates to allow floor plan financing interest to be fully deductible and to limit the deduction for net interest expense (less floor plan financing interest) to 30 percent of adjusted taxable income. That is, a deduction for business interest is permitted to the full extent of business interest income and any floor plan financing interest. To the extent that business interest exceeds business interest income and floor plan financing interest, the deduction for the net interest expense is limited to 30 percent of adjusted taxable income.[4] The House Report provides that it is generally intended that, similar to present law, section 163(j) apply after the application of provisions that subject interest to deferral, capitalization, or other limitation. Thus, section 163(j) applies to interest deductions that are deferred, for example under section 163(e) or section 267(a)(3)(B), in the taxable year to which such deductions are deferred.[5] The Report also provides that Section 163(j) applies after section 263A is applied to capitalize interest and after, for example, section 265 or section 279 is applied to disallow interest.[6]	The provision applies to taxable years beginning after December 31, 2017.	§ 163(j)

D.1. – LIMITATION ON BUSINESS INTEREST

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Miscellaneous itemized deductions that are not investment expenses are disallowed first before any investment expenses are disallowed. **<u>Earnings stripping</u>** Section 163(j) may disallow a deduction for disqualified interest paid or accrued by a corporation in a taxable year if two threshold tests are satisfied: the payor's debt-to-equity ratio exceeds 1.5 to 1.0 (the safe harbor ratio) and the payor's net interest expense exceeds 50 percent of its adjusted taxable income (generally, taxable income computed without regard to deductions for net interest expense, net operating losses, domestic production activities under section 199, depreciation, amortization, and depletion). Disqualified interest includes interest paid or accrued to: (1) related parties when no Federal income tax is imposed with respect to such interest; (2) unrelated parties in certain instances in which a related party guarantees the debt; or (3) to a real estate investment trust ("REIT") by a taxable REIT subsidiary of that trust. Interest amounts disallowed under these rules can be carried forward indefinitely. In addition, any excess limitation (*i.e.*, the excess, if any, of 50 percent of the adjusted taxable income of the payor over the payor's net interest expense) can be carried forward three years.	**2. Carryforward of Disallowed Business Interest.** The amount of any business interest not allowed as a deduction for any taxable year may be carried forward for up to five years beyond the year in which the business interest was paid or accrued. **3. Definition of Business Interest.** Business interest means any interest paid or accrued on indebtedness properly allocable to a trade or business.[7] Business interest does not include investment interest, and business interest income does not include investment income, within the meaning of section 163(d).[8] Any amount treated as interest for purposes of the Internal Revenue Code is interest for purposes of the provision.[9] The House Report notes that Section 163(d) applies in the case of a taxpayer other than a corporation. Thus, a corporation has neither investment interest nor investment income within the meaning of section 163(d). Thus, interest income and interest expense of a corporation is properly allocable to a trade or business, unless such trade or business is otherwise explicitly excluded from the application of the provision.[10] **4. Definition of Business Interest Income.** Business interest income means the amount of interest includible in the gross income of the taxpayer for the taxable year which is properly allocable to a trade or business.[11] **5. Adjusted Taxable Income.** Adjusted taxable income means the taxable income of the taxpayer computed without regard to: a. Any item of income, gain, deduction, or loss which is not properly allocable to a trade or business;[12]		§ 163(j)

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Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	b. Any business interest or business interest income. c. The amount of any net operating loss deduction;[13] d. Any deduction allowed under Section 199A;[14] and e. In the case of tax years beginning after December 31, 2017, and before January 1, 2022, any deduction allowable for depreciation, amortization, or depletion.[15] Any deduction allowable for depreciation, amortization, or depletion includes any deduction allowable for any amount treated as depreciation, amortization, or depletion under present law.[16] The statute grants Treasury the authority to provide other adjustments to the computation of adjusted taxable income.[17] **6. Definition of Floor Plan Financing.** Floor plan financing interest means interest paid or accrued on floor plan financing indebtedness. Floor plan financing indebtedness means indebtedness: a. Used to finance the acquisition of motor vehicles held for sale or lease;[19] and b. Secured by the inventory so acquired.[20] **7. Definition of Motor Vehicle.** A motor vehicle means a motor vehicle that is any of the following: a. Any self-propelled vehicle designed for transporting persons or property on a public street, highway, or road.[21] b. A boat.[22] c. Farm machinery or equipment.[23]		§ 163(j)

D.1. – LIMITATION ON BUSINESS INTEREST

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	8. Application to passthrough entities **a. In general.** In the case of any partnership, the limitation is applied at the partnership level.[24] Any deduction for business interest is taken into account in determining the nonseparately stated taxable income or loss of the partnership. To prevent double counting, special rules are provided for the determination of the adjusted taxable income of each partner of the partnership.[25] Similarly, to allow for an additional interest deduction by a partner in the case of an excess amount of unused adjusted taxable income limitation of the partnership, special rules apply.[26] Similar rules apply with respect to any S corporation and its shareholders.[27] **b. Double counting rule.** The adjusted taxable income of each partner (or shareholder, as the case may be) is determined without regard to such partner's distributive share of any items of income, gain, deduction or loss of the partnership.[28] In the absence of such a rule, the same dollars of adjusted taxable income of a partnership could generate additional interest deductions as the income is passed through to the partners.[29] **c. Additional deduction limit.** The limit on the amount allowed as a deduction for business interest is increased by a partner's distributive share of the partnership's excess taxable income.[30] The excess taxable income with respect to any partnership is the amount which bears the same ratio to the partnership's adjusted taxable income as the excess (if any) of 30 percent of the adjusted taxable income of the		§ 163(j)

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	partnership over the amount (if any) by which the business interest of the partnership, reduced by floor plan financing interest, exceeds the business interest income of the partnership bears to 30 percent of the adjusted taxable income of the partnership.[31] This allows a partner of a partnership to deduct additional interest expense the partner may have paid or incurred to the extent the partnership could have deducted more business interest.[32] Excess taxable income is required to be allocated in the same manner as nonseparately stated income and loss.[33] Rules similar to these rules also apply to S corporations.[34] **d. Carryforward of disallowed business interest.** The statute provides a special rule for carryforward of disallowed partnership interest.[35] In the case of a partnership, the general carryforward rule described above does not apply.[36] Instead, any business interest that is not allowed as a deduction to the partnership for the taxable year is treated as excess business interest and allocated to each partner in the same manner as nonseparately stated taxable income or loss of the partnership.[37] The partner may deduct its share of the partnership's excess business interest in the next succeeding year in which the partner is allocated excess taxable income from such partnership, but only to the extent of such excess taxable income. Any such deduction requires a corresponding reduction in excess taxable income.[38]		§ 163(j)

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	e. Basis Adjustments. **i. General Rule.** The adjusted basis of a partner in a partnership interest is reduced (but not below zero) by the amount of excess business interest allocated to such partner,[39] even though the carryforward does not give rise to a partner deduction in the year of the basis reduction.[40] However, the partner's deduction in a future year for interest carried forward does not reduce the partner's basis in the partnership interest.[41] **ii. Special Rule for Dispositions.** In the event the partner disposes of a partnership interest the basis of which has been so reduced, the partner's basis in such interest shall be increased, immediately before such disposition, by the amount that any such basis reductions exceed any amount of excess interest expense that has been treated as paid by the partner (*i.e.*, excess interest expense that has been deducted by the partner against excess taxable income of the same partnership).[42] This special rule does not apply to S corporations and their shareholders. Senate Report. This rule also applies to transfers of the partnership interest (including by reason of death) in a transaction in which gain is not recognized in whole or in part.[43] No deduction is allowed to the transferor or transferee for any excess business interest resulting in a basis increase.[44] **f. Exceptions.** The business interest limitation does not apply to any taxpayer (other than a tax shelter prohibited from using the cash receipts and disbursements method of accounting under Section 448(a)(3)) that meets the $25 million gross receipts test of section 448(c), that		§ 163(j)

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Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	is, if the average annual gross receipts for the three-taxable-year period ending with the prior taxable year does not exceed $25 million.692 Aggregation rules apply to determine the amount of a taxpayer's gross receipts under the gross receipts test of section 448(c).[45] In the case of a taxpayer which is not a corporation or partnership (e.g., sole proprietorship,[46] the $25 million gross receipts test is applied as if the sole proprietorship were a corporation or partnership.[47] **9. Trade or Business.** **a. Performing Services as an Employee is not a Trade or Business.** For purposes of the business interest limitation, the trade or business of performing services as an employee is not treated as a trade or business.[48] As a result, for example, the wages of an employee are not counted in the adjusted taxable income of the taxpayer for purposes of determining the limitation.[49] b. **Electing Real Property Trade or Business Not Treated as a Trade or Business.** Any electing real property trade or business is not treated as a trade or business for purposes of the limitation, and therefore the limitation does not apply to such trades or businesses.[50] The House Report states that "As a result, for example, interest expense paid or incurred in a real property trade or business is not business interest subject to limitation and is generally deductible in the computation of taxable income."[51] An "electing real property trade or business" means any trade or business which is described in Section 469(c)(7)(C) and which makes an election under Section 163(j)(7)(B) in		§ 163(j)

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	the manner prescribed by Treasury.[52] The real property trade or business described in Section 469(c)(7)(C) means any real property development, redevelopment, construction, reconstruction, acquisition, conversion, rental, operation, management, leasing, or brokerage trade or business.[53] The Senate Report states as follows: [I]t is intended that any such real property trade or business, including such a trade or business conducted by a corporation or real estate investment trust, be included. Because this description of a real property trade or business refers only to the section 469(c)(7)(C) description, and not to other rules of section 469 (such as the rule of section 469(c)(2) that passive activities include rental activities or the rule of section 469(a) that a passive activity loss is limited under section 469), the other rules of section 469 are not made applicable by this reference. It is further intended that a real property operation or a real property management trade or business includes the operation or management of a lodging facility. **c. Electing farming business.**[54] An electing farming business means: i. A farming business as defined in section 263A(e)(4) (*i.e.*, farming business means the trade or business of farming and includes the trade or business of operating a nursery or sod farm, or the raising or harvesting of trees bearing fruit, nuts, or other crops, or ornamental trees (other than evergreen trees that are more than six years old at the time they are		§ 163(j)

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	severed from their roots)) making an election under Section 163(j)(7)(C).[55] The Senate Report provides that Treas. Reg. sec. 1.263A-4(a)(4) further defines a farming business as a trade or business involving the cultivation of land or the raising or harvesting of any agricultural or horticultural commodity. Examples of a farming business include the trade or business of operating a nursery or sod farm; the raising or harvesting of trees bearing fruit, nuts, or other crops; the raising of ornamental trees (other than evergreen trees that are more than six years old at the time they are severed from their roots); and the raising, shearing, feeding, caring for, training, and management of animals. A farming business also includes processing activities that are normally incident to the growing, raising, or harvesting of agricultural or horticultural products. See Treas. Reg. sec. 1.263A- 4(a)(4)(i) and (ii). A farming business does not include contract harvesting of an agricultural or horticultural commodity grown or raised by another taxpayer, or merely buying and reselling plants or animals grown or raised by another taxpayer.[56] ii. Any trade or business of a specified agricultural or horticultural cooperative (as defined in Section 199A(g)(2)) which makes an election under Section 163(j)(7)(C). **d. Limitation Does Not Apply to Certain Regulated Public Utilities.** The limitation does not apply to certain regulated public utilities. Specifically, the trade or business of the furnishing or sale of (1) electrical energy, water, or sewage disposal services;[57] (2) gas or steam through a local distribution system;[58] or (3) transportation of gas or steam by pipeline,[59] if		§ 163(j)

D.1. – LIMITATION ON BUSINESS INTEREST

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	the rates for such furnishing or sale, as the case may be, have been established or approved by a State or political subdivision thereof, by any agency or instrumentality of the United States, or by a public service or public utility commission or other similar body of any State or political subdivision thereof, or by the governing body or ratemaking body of an electric cooperative, is not treated as a trade or business for purposes of the limitation.[60] [1] I.R.C. § 163(j)(2)(A). [2] I.R.C. § 163(j)(2(B). [3] I.R.C. § 163(j)(1). [4] House Report. [5] House Report. [6] House Report. [7] I.R.C. § 163(j)(5). [8] I.R.C. § 163(j)(5). [9] House Report. [10] House Report. [11] I.R.C. § 163(j)(6). [12] I.R.C. § 163(j)(8)(A)(ii). [13] I.R.C. § 163(j)(8)(A)(iii). [14] I.R.C. § 163(j)(8)(A)(iv). [15] I.R.C. § 163(j)(8)(A)(v). [16] House Report. [17] I.R.C. § 163(j)(2)(B). [18] I.R.C. § 163(j)(9)(A). [19] I.R.C. § 163(j)(9)(B)(i). [20] I.R.C. § 163(j)(9)(B)(ii). [21] I.R.C. § 163(j)(9)(C)(i). [22] I.R.C. § 163(j)(9)(C)(ii). [23] I.R.C. § 163(j)(9)(C)(iii). [24] I.R.C. § 163(j)(4)(A). [25] House Report; *see* I.R.C. § 163(j)(4)(A)(ii).		§ 163(j)

D.1. – LIMITATION ON BUSINESS INTEREST

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	[26] House Report; *see* I.R.C. § 163(j)(4)(A)(ii). [27] House Report; *see* I.R.C. § 163(j)(4)(D). [28] I.R.C. § 163(j)(4)(A)(ii)(I). [29] House Report. [30] I.R.C. § 163(j)(4)(A)(ii)(II). [31] I.R.C. § 163(j)(4)(C). [32] Senate Report. [33] I.R.C. § 163(j)(4)(A). [34] I.R.C. § 163(j)(4)(C). [35] *See* I.R.C. § 163(j)(4)(B). [36] I.R.C. § 163(j)(4)(B)(i)(I). [37] I.R.C. § 163(j)(4)(B). [38] I.R.C. § 163(j)(4)(B). [39] I.R.C. § 163(j)(4)(B)(iii)(I). [40] Senate Amendment. [41] Senate Amendment. [42] I.R.C. § 163(j)(4)(B)(iii)(II); Senate Report. [43] I.R.C. § 163(j)(4)(B)(iii)(II). [44] I.R.C. § 163(j)(4)(B)(iii)(II). [45] Senate amendment; *see* I.R.C. § 448(c)(2). [46] House Report. [47] I.R.C. § 163(j)(3). [48] I.R.C. § 163(j)(7)(A)(i). [49] House Report. [50] I.R.C. § 163(j)(7)(A)(ii). [51] House Report. [52] I.R.C. § 163(j)(7)(B). [53] I.R.C. § 469(c)(7)(C). [54] I.R.C. § 163(j)(7)(A)(iii). [55] I.R.C. § 163(j)(7)(C). [56] Senate Report. [57] I.R.C. § 163(j)(7)(A)(iv)(I). [58] I.R.C. § 163(j)(7)(A)(iv)(II). [59] I.R.C. § 163(j)(7)(A)(iv)(III). [60] I.R.C. § 163(j)(7).		§ 163(j)

D.2. –MODIFICATION OF NET OPERATING LOSS DEDUCTION

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
A net operating loss ("NOL") generally means the amount by which a taxpayer's business deductions exceed its gross income. In general, an NOL may be carried back two years and carried over 20 years to offset taxable income in such years. NOLs offset taxable income in the order of the taxable years to which the NOL may be carried. Different carryback periods apply with respect to NOLs arising in different circumstances. Extended carryback periods are allowed for NOLs attributable to specified liability losses and certain casualty and disaster losses. Limitations are placed on the carryback of excess interest losses attributable to corporate equity reduction transactions.	The provision limits the NOL deduction to 80 percent of taxable income (determined without regard to the deduction), for loses arising in taxable years beginning after December 31, 2017.[1] The limitation does not apply to a property and casualty insurance company. Carryovers to other years are adjusted to take account of this limitation, and may be carried forward indefinitely.[2] The provision repeals the two-year carryback and the special carryback provisions, but provides a two-year carryback in the case of certain losses incurred in the trade or business of farming.[3] It provides a two-year carryback and 20-year carryforward for NOLs of a property and casualty insurance company (defined in section 816(a)) as an insurance company other than a life insurance company).[4] The provision does not increase NOL carryovers. [1] IRC § 172(a). [2] IRC § 172(f). [3] IRC § (b)(1)(B). [4] IRC § 172(b)(1)(C).	The provisions apply to losses arising in taxable years beginning after December 31, 2017.	§ 172

D.3. – LIKE-KIND EXCHANGES OF REAL PROPERTY

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
An exchange of property, like a sale, generally is a taxable event. However, no gain or loss is recognized if property held for productive use in a trade or business or for investment is exchanged for property of a “like kind” which is to be held for productive use in a trade or business or for investment. In general, section 1031 does not apply to any exchange of stock in trade (*i.e.*, inventory) or other property held primarily for sale; stocks, bonds, or notes; other securities or evidences of indebtedness or interest; interests in a partnership; certificates of trust or beneficial interests; or choses in action. Section 1031 also does not apply to certain exchanges involving livestock or foreign property. For purposes of section 1031, the determination of whether property is of a “like kind” relates to the nature or character of the property and not its grade or quality, *i.e.*, the nonrecognition rules do not apply to an exchange of one class or kind of property for property of a different class or kind (e.g., section 1031 does not apply to an exchange of real property for personal property). The different classes of property are: (1) depreciable tangible personal property; (2) intangible or nondepreciable personal property; and (3) real property. However, the rules with respect to whether real estate is “like kind” are applied more liberally than the rules governing like-kind exchanges of depreciable, intangible, or nondepreciable personal property. For example, improved real estate and unimproved real estate generally are considered to be property of a “like kind” as this distinction relates to the grade or quality of the real estate, while depreciable tangible personal properties must be either within the same General Asset Class or within the same Product Class.	The Act modifies the provision providing for nonrecognition of gain in the case of like-kind exchanges by limiting its application to real property[1] that is not held primarily for sale.[2] [1] I.R.C. § 1031(a)(1). [2] I.R.C. § 1031(a)(2). [3] Tax Cuts and Jobs Act § 13303(c)(1). [4] Tax Cuts and Jobs Act § 13303(c)(2).	The provision generally applies to exchanges completed after December 31, 2017.[3] However, an exception is provided for any exchange if the property disposed of by the taxpayer in the exchange is disposed of on or before December 31, 2017, or the property received by the taxpayer in the exchange is received on or before such date.[4]	§ 1031

D.4. - REVISION OF TREATMENT OF CONTRIBUTIONS TO CAPITAL

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
The gross income of a corporation does not include any contribution to its capital. For purposes of this rule, a contribution to the capital of a corporation does not include any contribution in aid of construction or any other contribution from a customer or potential customer. A special rule allows certain contributions in aid of construction received by a regulated public utility that provides water or sewerage disposal services to be treated as a tax-free contribution to the capital of the utility. No deduction or credit is allowed for, or by reason of, any expenditure that constitutes a contribution that is treated as a tax-free contribution to the capital of the utility. If property is acquired by a corporation as a contribution to capital and is not contributed by a shareholder as such, the adjusted basis of the property is zero. If the contribution consists of money, the corporation must first reduce the basis of any property acquired with the contributed money within the following 12-month period, and then reduce the basis of other property held by the corporation. Similarly, the adjusted basis of any property acquired by a utility with a contribution in aid of construction is zero.	The provision continues to exclude contributions to capital from the gross income of a corporation. However, the provision provides that the term “contributions to capital” does not include (1) any contribution in aid of construction or any other contribution as a customer or potential customer, and (2) any contribution by any governmental entity or civic group (other than a contribution made by a shareholder as such).	The provision applies to contributions made after the date of enactment. However, the provision shall not apply to any contribution made after the date of enactment by a governmental entity pursuant to a master development plan that has been approved prior to such date by a governmental entity.	§ 118

D.5. - REPEAL OF DEDUCTION FOR LOCAL LOBBYING EXPENSES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
In general A taxpayer generally is allowed a deduction for ordinary and necessary expenses paid or incurred in carrying on any trade or business. However, section 162(e) denies a deduction for amounts paid or incurred in connection with (1) influencing legislation, (2) participation in, or intervention in, any political campaign on behalf of (or in opposition to) any candidate for public office, (3) any attempt to influence the general public, or segments thereof, with respect to elections, legislative matters, or referendums, or (4) any direct communication with a covered executive branch official in an attempt to influence the official actions or positions of such official. Expenses paid or incurred in connection with lobbying and political activities (such as research for, or preparation, planning, or coordination of, any previously described activity) also are not deductible. **Exceptions** **Local legislation** Notwithstanding the above, a deduction is allowed for ordinary and necessary expenses incurred in connection with any legislation of any local council or similar governing body ("local legislation"). With respect to local legislation, the exception permits a deduction for amounts paid or incurred in carrying on any trade or business (1) in direct connection with appearances before, submission of statements to, or sending communications to the committees or individual members of such council or body with respect to legislation or proposed legislation of direct interest to the taxpayer, or (2) in direct connection with communication of information between the taxpayer and an organization of which the taxpayer is a	The provision denies a deduction for amounts paid related to lobbying local councils or similar governing bodies, including Indian tribal governments.[1] Thus, the general disallowance rules applicable to lobbying and political expenditures will apply to costs incurred related to such local legislation. [1] I.R.C. § 162(e)	The provision applies to amounts paid or incurred after December 31, 2017.	§ 162(e)

D.5. - REPEAL OF DEDUCTION FOR LOCAL LOBBYING EXPENSES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
member with respect to any such legislation or proposed legislation which is of direct interest to the taxpayer and such organization, and (3) that portion of the dues paid or incurred with respect to any organization of which the taxpayer is a member which is attributable to the expenses of the activities described in (1) or (2) carried on by such organization. For purposes of this exception, legislation of an Indian tribal government is treated in the same manner as local legislation. **De minimis** For taxpayers with $2,000 or less of in-house expenditures related to lobbying and political activities, a de minimis exception is provided that permits a deduction.			§ 162(e)

D.6. - REPEAL OF 199 DEDUCTION

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
In general Section 199 provides a deduction from taxable income (or, in the case of an individual, adjusted gross income) that is equal to nine percent of the lesser of the taxpayer's qualified production activities income or taxable income (determined without regard to the section 199 deduction) for the taxable year. For corporations subject to the 35-percent corporate income tax rate, the nine-percent deduction effectively reduces the corporate income tax rate to slightly less than 32 percent on qualified production activities income. A similar reduction applies to the graduated rates applicable to individuals with qualifying domestic production activities income. In general, qualified production activities income is equal to domestic production gross receipts reduced by the sum of: (1) the costs of goods sold that are allocable to those receipts; and (2) other expenses, losses, or deductions which are properly allocable to those receipts. Domestic production gross receipts generally are gross receipts of a taxpayer that are derived from: (1) any sale, exchange, or other disposition, or any lease, rental, or license, of qualifying production property that was manufactured, produced, grown or extracted by the taxpayer in whole or in significant part within the United States; (2) any sale, exchange, or other disposition, or any lease, rental, or license, of qualified film produced by the taxpayer; (3) any sale, exchange, or other disposition, or any lease, rental, or license, of electricity, natural gas, or potable water produced by the taxpayer in the United States; (4) construction of real property performed in the United States by a taxpayer in the ordinary course of a construction trade or business; or	**Repeal of deduction for income attributable to domestic production activities.** The provision repeals the deduction for income attributable to domestic production activities.[1] [1] Tax Cuts and Jobs Act § 13305(a)	The provision is applicable to taxable years beginning after December 31, 2017.	N/A

D.6. - REPEAL OF 199 DEDUCTION

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
(5) engineering or architectural services performed in the United States for the construction of real property located in the United States. The amount of the deduction for a taxable year is limited to 50 percent of the W-2 wages paid by the taxpayer, and properly allocable to domestic production gross receipts, during the calendar year that ends in such taxable year. **<u>Agricultural and horticultural cooperatives</u>** With regard to member-owned agricultural and horticultural cooperatives formed under Subchapter T of the Code, section 199 provides the same treatment of qualified production activities income derived from agricultural or horticultural products that are manufactured, produced, grown, or extracted by cooperatives, or that are marketed through cooperatives, as it provides for qualified production activities income of other taxpayers (*i.e.*, the cooperative may claim a deduction from qualified production activities income). In addition, section 199(d)(3)(A) provides that the amount of any patronage dividends or per-unit retain allocations paid to a member of an agricultural or horticultural cooperative (to which Part I of Subchapter T applies), which is allocable to the portion of qualified production activities income of the cooperative that is deductible under the provision, is deductible from the gross income of the member. In order to qualify, such amount must be designated by the organization as allocable to the deductible portion of qualified production activities income in a written notice mailed to its patrons not later than the payment period described in section 1382(d). In addition, section 199(d)(3)(B) provides that the cooperative cannot reduce its income under section 1382 (*e.g.*, cannot claim a dividends-paid deduction) for such amounts.			N/A

D.7. - DENIAL OF DEDUCTIONS FOR ENTERTAINMENT, ETC. EXPENSES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
In general No deduction is allowed with respect to (1) an activity generally considered to be entertainment, amusement, or recreation ("entertainment"), unless the taxpayer establishes that the item was directly related to (or, in certain cases, associated with) the active conduct of the taxpayer's trade or business, or (2) a facility (e.g., an airplane) used in connection with such activity. If the taxpayer establishes that entertainment expenses are directly related to (or associated with) the active conduct of its trade or business, the deduction generally is limited to 50 percent of the amount otherwise deductible. Similarly, a deduction for any expense for food or beverages generally is limited to 50 percent of the amount otherwise deductible. In addition, no deduction is allowed for membership dues with respect to any club organized for business, pleasure, recreation, or other social purpose. There are a number of exceptions to the general rule disallowing deduction of entertainment expenses and the rules limiting deductions to 50 percent of the otherwise deductible amount. Under one such exception, those rules do not apply to expenses for goods, services, and facilities to the extent that the expenses are reported by the taxpayer as compensation and as wages to an employee. Those rules also do not apply to expenses for goods, services, and facilities to the extent that the expenses are includible in the gross income of a recipient who is not an employee (*e.g.*, a nonemployee director) as compensation for services rendered or as a prize or award. The exceptions apply only to the extent that amounts are properly reported by the company as compensation and wages or otherwise includible in income.	1. The provision provides that no deduction is allowed with respect to (1) an activity generally considered to be entertainment, amusement or recreation, (2) membership dues with respect to any club organized for business, pleasure, recreation or other social purposes, or (3) a facility or portion thereof used in connection with any of the above items.[1] Thus, the provision repeals the present-law exception to the deduction disallowance for entertainment, amusement, or recreation that is directly related to (or, in certain cases, associated with) the active conduct of the taxpayer's trade or business (and the related rule applying a 50 percent limit to such deductions). 2. In addition, the provision disallows a deduction for expenses associated with providing any qualified transportation fringe to employees of the taxpayer,[2] and except as necessary for ensuring the safety of an employee, any expense incurred for providing transportation (or any payment or reimbursement) for commuting between the employee's residence and place of employment.[3] 3. Taxpayers may still generally deduct 50 percent of the food and beverage expenses associated with operating their trade or business (*e.g.*, meals consumed by employees on work travel). For amounts incurred and paid after December 31, 2017 and until December 31, 2025,[4] the provision expands this 50 percent limitation to expenses of the employer associated with providing food and beverages to employees through an eating facility that meets requirements for *de minimis* fringes and for the convenience of the employer.[5] Such amounts incurred and paid after December 31, 2025 are not deductible.	The provision generally applies to amounts paid or incurred after December 31, 2017. However, for expenses of the employer associated with providing food and beverages to employees through an eating facility that meets requirements for de minimis fringes and for the convenience of the employer, amounts paid or incurred after December 31, 2025 are not deductible.	§ 274

D.7. - DENIAL OF DEDUCTIONS FOR ENTERTAINMENT, ETC. EXPENSES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
In no event can the amount of the deduction exceed the amount of the taxpayer's actual cost, even if a greater amount (i.e., fair market value) is includible in income. Those deduction disallowance rules also do not apply to expenses paid or incurred by the taxpayer, in connection with the performance of services for another person (other than an employer), under a reimbursement or other expense allowance arrangement if the taxpayer accounts for the expenses to such person. Another exception applies for expenses for recreational, social, or similar activities primarily for the benefit of employees other than certain owners and highly compensated employees. An exception applies also to the 50 percent deduction limit for food and beverages provided to crew members of certain commercial vessels and certain oil or gas platform or drilling rig workers. **<u>Expenses treated as compensation</u>** Except as otherwise provided, gross income includes compensation for services, including fees, commissions, fringe benefits, and similar items. In general, an employee (or other service provider) must include in gross income the amount by which the fair market value of a fringe benefit exceeds the sum of the amount (if any) paid by the individual and the amount (if any) specifically excluded from gross income. Treasury regulations provide detailed rules regarding the valuation of certain fringe benefits, including flights on an employer-provided aircraft. In general, the value of a non-commercial flight generally is determined under the base aircraft valuation formula, also known as the Standard Industry Fare Level formula or "SIFL." If the SIFL	[1] I.R.C. § 274(a)(1). [2] I.R.C. § 274(a)(4). [3] I.R.C. § 274(l) [4] I.R.C. § 274(n). [5] I.R.C. § 274(e).		§ 274

D.7. - DENIAL OF DEDUCTIONS FOR ENTERTAINMENT, ETC. EXPENSES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
valuation rules do not apply, the value of a flight on an employer-provided aircraft generally is equal to the amount that an individual would have to pay in an arm's-length transaction to charter the same or a comparable aircraft for that period for the same or a comparable flight. In the context of an employer providing an aircraft to employees for nonbusiness (e.g., vacation) flights, the exception for expenses treated as compensation has been interpreted as not limiting the company's deduction for expenses attributable to the operation of the aircraft to the amount of compensation reportable to its employees. The result of that interpretation is often a deduction several times larger than the amount required to be included in income. Further, in many cases, the individual including amounts attributable to personal travel in income directly benefits from the enhanced deduction, resulting in a net deduction for the personal use of the company aircraft. The exceptions for expenses treated as compensation or otherwise includible income were subsequently modified in the case of specified individuals such that the exceptions apply only to the extent of the amount of expenses treated as compensation or includible in income of the specified individual. Specified individuals are individuals who, with respect to an employer or other service recipient (or a related party), are subject to the requirements of section 16(a) of the Securities Exchange Act of 1934, or would be subject to such requirements if the employer or service recipient (or related party) were an issuer of equity securities referred to in section 16(a).			§ 274

D.7. - DENIAL OF DEDUCTIONS FOR ENTERTAINMENT, ETC. EXPENSES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
As a result, in the case of specified individuals, no deduction is allowed with respect to expenses for (1) a nonbusiness activity generally considered to be entertainment, amusement or recreation, or (2) a facility (*e.g.*, an airplane) used in connection with such activity to the extent that such expenses exceed the amount treated as compensation or includible in income to the specified individual. For example, a company's deduction attributable to aircraft operating costs and other expenses for a specified individual's vacation use of a company aircraft is limited to the amount reported as compensation to the specified individual. However, in the case of other employees or service providers, the company's deduction is not limited to the amount treated as compensation or includible in income. **<u>Excludable fringe benefits</u>** Certain employer-provided fringe benefits are excluded from an employee's gross income and wages for employment tax purposes, including, but not limited to, de minimis fringes, qualified transportation fringes, on-premises athletic facilities, and meals provided for the "convenience of the employer." Qualified transportation fringes include qualified parking (parking on or near the employer's business premises or on or near a location from which the employee commutes to work by public transit), transit passes, vanpool benefits, and qualified bicycle commuting reimbursements. On-premises athletic facilities are gyms or other athletic facilities located on the employer's premises, operated by the employer, and substantially all the use of which is by employees of the employer, their spouses, and their dependent children.			§ 274

D.7. - DENIAL OF DEDUCTIONS FOR ENTERTAINMENT, ETC. EXPENSES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
The value of meals furnished to an employee or the employee's spouse or dependents by or on behalf of an employer for the convenience of the employer is excludible from the employee's gross income, but only if such meals are provided on the employer's business premises.			§ 274

D.9. - UNRELATED BUSINESS TAXABLE INCOME INCREASED BY AMOUNT OF CERTAIN FRINGE BENEFIT EXPENSES FOR WHICH A DEDUCTION IS DISALLOWED

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
<u>Tax exemption for certain organizations</u> Section 501(a) exempts certain organizations from Federal income tax. Such organizations include: (1) tax-exempt organizations described in section 501(c) (including among others section 501(c)(3) charitable organizations and section 501(c)(4) social welfare organizations); (2) religious and apostolic organizations described in section 501(d); and (3) trusts forming part of a pension, profit-sharing, or stock bonus plan of an employer described in section 401(a). **<u>Unrelated business income tax, in general</u>** The unrelated business income tax ("UBIT") generally applies to income derived from a trade or business regularly carried on by the organization that is not substantially related to the performance of the organization's tax-exempt functions. An organization that is subject to UBIT and that has $1,000 or more of gross unrelated business taxable income must report that income on Form 990-T (Exempt Organization Business Income Tax Return). Most exempt organizations may operate an unrelated trade or business so long as the organization remains primarily engaged in activities that further its exempt purposes. Therefore, an organization may engage in a substantial amount of unrelated business activity without jeopardizing its exempt status. A section 501(c)(3) (charitable) organization, however, may not operate an unrelated trade or business as a substantial part of its activities. Therefore, the unrelated trade or business activity of a section 501(c)(3) organization must be insubstantial.	Under the provision, unrelated business taxable income includes any expenses paid or incurred by a tax exempt organization for qualified transportation fringe benefits (as defined in section 132(f)), a parking facility used in connection with qualified parking (as defined in section 132(f)(5)(C)), or any on-premises athletic facility (as defined in section 132(j)(4)(B)), provided such amounts are not deductible under section 274.	The provision is effective for amounts paid or incurred after December 31, 2017.	§ 512

D.9. - UNRELATED BUSINESS TAXABLE INCOME INCREASED BY AMOUNT OF CERTAIN FRINGE BENEFIT EXPENSES FOR WHICH A DEDUCTION IS DISALLOWED

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
An organization determines its unrelated business taxable income by subtracting from its gross unrelated business income deductions directly connected with the unrelated trade or business. Under regulations, in determining unrelated business taxable income, an organization that operates multiple unrelated trades or businesses aggregates income from all such activities and subtracts from the aggregate gross income the aggregate of deductions. As a result, an organization may use a loss from one unrelated trade or business to offset gain from another, thereby reducing total unrelated business taxable income. **<u>Organizations subject to tax on unrelated business income</u>** Most exempt organizations are subject to the tax on unrelated business income. Specifically, organizations subject to the unrelated business income tax generally include: (1) organizations exempt from tax under section 501(a), including organizations described in section 501(c) (except for U.S. instrumentalities and certain charitable trusts); (2) qualified pension, profit-sharing, and stock bonus plans described in section 401(a); and (3) certain State colleges and universities. **<u>Exclusions from Unrelated Business Taxable Income</u>** Certain types of income are specifically exempt from unrelated business taxable income, such as dividends, interest, royalties, and certain rents, unless derived from debt-financed property or from certain 50-percent controlled subsidiaries.			§ 512

D.9. - UNRELATED BUSINESS TAXABLE INCOME INCREASED BY AMOUNT OF CERTAIN FRINGE BENEFIT EXPENSES FOR WHICH A DEDUCTION IS DISALLOWED

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Other exemptions from UBIT are provided for activities in which substantially all the work is performed by volunteers, for income from the sale of donated goods, and for certain activities carried on for the convenience of members, students, patients, officers, or employees of a charitable organization. In addition, special UBIT provisions exempt from tax activities of trade shows and State fairs, income from bingo games, and income from the distribution of low-cost items incidental to the solicitation of charitable contributions. Organizations liable for tax on unrelated business taxable income may be liable for alternative minimum tax determined after taking into account adjustments and tax preference items.			§ 512

D.10 – LIMITATION ON DEDUCTION FOR FDIC PREMIUMS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Corporations organized under the laws of any of the 50 States (and the District of Columbia) generally are subject to the U.S. corporate income tax on their worldwide taxable income. The taxable income of a C corporation generally comprises gross income less allowable deductions. A taxpayer generally is allowed a deduction for ordinary and necessary expenses paid or incurred in carrying on any trade or business. Corporations that make a valid election pursuant to section 1362 of subchapter S of the Code, referred to as S corporations, generally are not subject to corporate-level income tax on its items of income and loss. Instead, an S corporation passes through to shareholders its items of income and loss. The shareholders separately take into account their shares of these items on their individual income tax returns. **<u>Banks, thrifts, and credit unions</u>** **<u>In general</u>** Financial institutions are subject to the same Federal income tax rules and rates as are applied to other corporations or entities, with specified exceptions. **<u>C corporation banks and thrifts</u>** A bank is generally taxed for Federal income tax purposes as a C corporation. For this purpose a bank generally means a corporation, a substantial portion of whose business is receiving deposits and making loans and discounts, or exercising certain fiduciary powers. A bank for this purpose generally includes domestic building and loan associations, mutual stock or savings banks, and certain cooperative banks that are commonly referred to as thrifts.	1. No deduction is allowed for the applicable percentage of any FDIC premium paid or incurred by the taxpayer.[1] For taxpayers with total consolidated assets of $50 billion or more, the applicable percentage is 100 percent. Otherwise, the applicable percentage is the ratio of the excess of total consolidated assets over $10 billion to $40 billion. For example, for a taxpayer with total consolidated assets of $20 billion, no deduction is allowed for 25 percent of FDIC premiums. The provision does not apply to taxpayers with total consolidated assets (as of the close of the taxable year) that do not exceed $10 billion.[2] 2. FDIC premium means any assessment imposed under section 7(b) of the Federal Deposit Insurance Act. The term total consolidated assets has the meaning given such term under section 165 of the Dodd-Frank Wall Street Reform and Consumer Protection Act. 3. For purposes of determining a taxpayer's total consolidated assets, members of an expanded affiliated group are treated as a single taxpayer. An expanded affiliated group means an affiliated group as defined in section 1504(a), determined by substituting "more than 50 percent" for "at least 80 percent" each place it appears and without regard to the exceptions from the definition of includible corporation for insurance companies and foreign corporations. A partnership or any other entity other than a corporation is treated as a member of an expanded affiliated group if such entity is controlled by members of such group.[3]	The provision applies to taxable years beginning after December 31, 2017	§ 162

D.10 – LIMITATION ON DEDUCTION FOR FDIC PREMIUMS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
S corporation banks A bank is generally eligible to elect S corporation status under section 1362, provided it meets the other requirements for making this election and it does not use the reserve method of accounting for bad debts as described in section 585. **Special bad debt loss rules for small banks** Section 166 provides a deduction for any debt that becomes worthless (wholly or partially) within a taxable year. The reserve method of accounting for bad debts, repealed in 1986 for most taxpayers, is allowed under section 585 for any bank (as defined in section 581) other than a large bank. For this purpose, a bank is a large bank if, for the taxable year (or for any preceding taxable year after 1986), the average adjusted basis of all its assets (or the assets of the controlled group of which it is a member) exceeds $500 million. Deductions for reserves are taken in lieu of a worthless debt deduction under section 166. Accordingly, a small bank is able to take deductions for additions to a bad debt reserve. Additions to the reserve are determined under an experience method that generally looks to the ratio of (1) the total bad debts sustained during the taxable year and the five preceding taxable years to (2) the sum of the loans outstanding at the close of such taxable years. **Credit unions** Credit unions are exempt from Federal income taxation. The exemption is based on their status as not-for-profit mutual or cooperative organizations (without capital stock) operated for the benefit of their members, who generally must share a common	[1] I.R.C. § 162(r). [2] I.R.C. § 162(r)(3). [3] I.R.C. § 162(r)(6).		§ 162

D.10 – LIMITATION ON DEDUCTION FOR FDIC PREMIUMS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
bond. The definition of common bond has been expanded to permit greater use of credit unions. While significant differences between the rules under which credit unions and banks operate have existed in the past, most of those differences have disappeared over time. **FDIC premiums** The Federal Deposit Insurance Corporation ("FDIC") provides deposit insurance for banks and savings institutions. To maintain its status as an insured depository institution, a bank must pay semiannual assessments into the deposit insurance fund ("DIF"). Assessments for deposit insurance are treated as ordinary and necessary business expenses. These assessments, also known as premiums, are deductible once the all events test for the premium is satisfied.			§ 162

D.11. - REPEAL OF ROLLOVER OF PUBLICLY TRADED SECURITIES GAIN INTO SPECIALIZED SMALL BUSINESS INVESTMENT COMPANIES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
A corporation or individual may elect to roll over tax-free any capital gain realized on the sale of publicly-traded securities to the extent of the taxpayer's cost of purchasing common stock or a partnership interest in a specialized small business investment company within 60 days of the sale. The amount of gain that an individual may elect to roll over under this provision for a taxable year is limited to (1) $50,000 or (2) $500,000 reduced by the gain previously excluded under this provision. For corporations, these limits are $250,000 and $1 million, respectively.	**Repeal of Rollover of Publicly-Traded Securities Gain Into Specialized Small Business Investment Companies.** The Act repeals the election described above to roll over tax-free capital gain realized on the sale of publicly-traded securities.[1] [1] Act Sec. 13313(a) [2] Act Sec. 13313(c)	The provision applies to sales after December 31, 2017.[2]	§ 1044

D.14. – REPEAL OF TECHNICAL TERMINATION OF PARTNERSHIPS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
A partnership is considered as terminated under specified circumstances. Special rules apply in the case of the merger, consolidation, or division of a partnership. A partnership is treated as terminated if no part of any business, financial operation, or venture of the partnership continues to be carried on by any of its partners in a partnership. A partnership is also treated as terminated if within any 12-month period, there is a sale or exchange of 50 percent or more of the total interest in partnership capital and profits. This is sometimes referred to as a technical termination. Under regulations, the technical termination gives rise to a deemed contribution of all the partnership's assets and liabilities to a new partnership in exchange for an interest in the new partnership, followed by a deemed distribution of interests in the new partnership to the purchasing partners and the other remaining partners. The effect of a technical termination is not necessarily the end of the partnership's existence, but rather the termination of some tax attributes. Upon a technical termination, the partnership's taxable year closes, potentially resulting in short taxable years. Partnership-level elections generally cease to apply following a technical termination. A technical termination generally results in the restart of partnership depreciation recovery periods.	The provision repeals the section 708(b)(1)(B) rule providing for technical terminations of partnerships where there is a sale or exchange of 50-percent or more of the total interest in the partnership.[1] The provision does not change the present-law rule of section 708(b)(1)(A) that a partnership is considered as terminated if no part of any business, financial operation, or venture of the partnership continues to be carried on by any of its partners in a partnership.[2] The provision applies to partnership taxable years beginning after December 31, 2017.[3] [1] Tax Cuts and Jobs Act § 13504(a); *see* I.R.C. § 708(b)(1); I.R.C. § 708(b)(1) (prior to Amendment by the Tax Cuts and Jobs Act). [2] I.R.C. § 708(b)(1). [3] Tax Cuts and Jobs Act § 13504(c).		§ 708(b)

D.15. - RECHARACTERIZATION OF CERTAIN GAINS IN THE CASE OF PARTNERSHIP PROFITS INTERESTS HELD IN CONNECTION WITH PERFORMANCE OF INVESTMENT SERVICES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
<u>Partnership profits interest for services</u> A profits interest in a partnership is the right to receive future profits in the partnership but does not generally include any right to receive money or other property upon the immediate liquidation of the partnership. The treatment of the receipt of a profits interest in a partnership (sometimes referred to as a carried interest) in exchange for the performance of services has been the subject of controversy. Though courts have differed, in some instances, a taxpayer receiving a profits interest for performing services has not been taxed upon the receipt of the partnership interest. In 1993, the Internal Revenue Service, referring to the litigation of the tax treatment of receiving a partnership profits interest and the results in the cases, issued administrative guidance that the IRS generally would treat the receipt of a partnership profits interest for services as not a taxable event for the partnership or the partner. Under this guidance, this treatment does not apply, however, if: (1) the profits interest relates to a substantially certain and predictable stream of income from partnership assets, such as income from high-quality debt securities or a high- quality net lease; (2) within two years of receipt, the partner disposes of the profits interest; or (3) the profits interest is a limited partnership interest in a publicly traded partnership. More recent administrative guidance clarifies that this treatment applies with respect to substantially unvested profits interests provided the service partner takes into income his distributive share of partnership income, and the partnership does not deduct any amount either on grant or on vesting of the profits interest.	**1. General rule.** The provision provides for a three-year holding period in the case of certain net long-term capital gain with respect to any applicable partnership interest held by the taxpayer.[1] The provision treats as short-term capital gain taxed at ordinary income rates the amount of the taxpayer's net long-term capital gain with respect to an applicable partnership interest for the taxable year that exceeds the amount of such gain calculated as if a three-year (not one-year) holding period applies, notwithstanding the rules of section 83 or any election in effect under section 83(b).[2] In making this calculation, the provision takes account of long-term capital losses calculated as if a three-year holding period applies.[3] The Conference Report provides that the conferees wish to clarify the interaction of section 83 with the provision's three-year holding requirement, which applies notwithstanding the rules of section 83 or any election in effect under section 83(b). Under the provision, the fact that an individual may have included an amount in income upon acquisition of the applicable partnership interest, or that an individual may have made a section 83(b) election with respect to an applicable partnership interest, does not change the three-year holding period requirement for long-term capital gain treatment with respect to the applicable partnership interest. Thus, the provision treats as short-term capital gain taxed at ordinary income rates the amount of the	The provision applies to taxable years beginning after December 31, 2017.[29]	§ 1061 § 83

D.15. - RECHARACTERIZATION OF CERTAIN GAINS IN THE CASE OF PARTNERSHIP PROFITS INTERESTS HELD IN CONNECTION WITH PERFORMANCE OF INVESTMENT SERVICES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
By contrast, a partnership capital interest received for services is includable in the partner's income under generally applicable rules relating to the receipt of property for the performance of services. A partnership capital interest for this purpose is an interest that would entitle the receiving partner to a share of the proceeds if the partnership's assets were sold at fair market value and the proceeds were distributed in liquidation. **<u>Property received for services under section 83</u>** **<u>In general</u>** Section 83 governs the amount and timing of income and deductions attributable to transfers of property in connection with the performance of services. If property is transferred in connection with the performance of services, the person performing the services (the "service provider") generally must recognize income for the taxable year in which the property is first substantially vested (*i.e.*, transferable or not subject to a substantial risk of forfeiture). The amount includible in the service provider's income is the excess of the fair market value of the property over the amount (if any) paid for the property. A deduction is allowed to the person for whom such services are performed (the "service recipient") equal to the amount included in gross income by the service provider. The deduction is allowed for the taxable year of the service recipient in which or with which ends the taxable year in which the amount is included in the service provider's income. Property that is subject to a substantial risk of forfeiture and that is not transferable is generally	taxpayer's net long-term capital gain with respect to an applicable partnership interest for the taxable year that exceeds the amount of such gain calculated as if a three-year (not one-year) holding period applies. In making this calculation, the provision takes account of long-term capital losses calculated as if a three-year holding period applies.[4] **2. Special Rule Concerning Portfolio Investment on Behalf of Third Party Investors.** A special rule provides that, to the extent provided in guidance by Treasury, the holding period rule does not apply to income or gain attributable to any asset that is not held for portfolio investment on behalf of third party investors.[5] Third party investor means a person (1) who holds an interest in the partnership that is not property held in connection with an applicable trade or business (defined below) with respect to that person,[6] and (2) who is not and has not been actively engaged in directly or indirectly providing substantial services for the partnership or any applicable trade or business (and is (or was) not related to a person so engaged).[7] A related person for this purpose is a family member (within the meaning of attribution rules) or colleague, that is a person who performed a service within the current calendar year or the preceding three calendar years in any applicable trade or business in which or for which the taxpayer performed a service.[8]		§ 1061 § 83

D.15. - RECHARACTERIZATION OF CERTAIN GAINS IN THE CASE OF PARTNERSHIP PROFITS INTERESTS HELD IN CONNECTION WITH PERFORMANCE OF INVESTMENT SERVICES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
referred to as "substantially nonvested." Property is subject to a substantial risk of forfeiture if the individual's right to the property is conditioned on the future performance (or refraining from performance) of substantial services. In addition, a substantial risk of forfeiture exists if the right to the property is subject to a condition other than the performance of services, provided that the condition relates to a purpose of the transfer and there is a substantial possibility that the property will be forfeited if the condition does not occur. **<u>Section 83(b) election</u>** Under section 83(b), even if the property is substantially nonvested at the time of transfer, the service provider may nevertheless elect within 30 days of the transfer to recognize income for the taxable year of the transfer. Such an election is referred to as a "section 83(b) election." The service provider makes an election by filing with the IRS a written statement that includes the fair market value of the property at the time of transfer and the amount (if any) paid for the property. The service provider must also provide a copy of the statement to the service recipient. **<u>Passthrough tax treatment of partnerships</u>** The character of partnership items passes through to the partners, as if the items were realized directly by the partners. Thus, for example, long-term capital gain of the partnership is treated as long-term capital gain in the hands of the partners. A partner holding a partnership interest includes in income its distributive share (whether or not	**3. Applicable partnership interest.** An applicable partnership interest is any interest in a partnership that, directly or indirectly, is transferred to (or held by) the taxpayer in connection with performance of substantial services in any applicable trade or business. The services may be performed by the taxpayer or by any other related person or persons in any applicable trade or business.[9] It is intended that partnership interests shall not fail to be treated as transferred or held in connection with the performance of services merely because the taxpayer also made contributions to the partnership, and the Treasury Department is directed to provide guidance implementing this intent.[10] An applicable partnership interest does not include an interest held by a person who is employed by another entity that is conducting a trade or business (which is not an applicable trade or business) and who provides services only to the other entity.[11] **4. Exceptions.** **a. Partnership Held by Corporation.** An applicable partnership interest does not include an interest in a partnership directly or indirectly held by a corporation.[12] For example, if two corporations form a partnership to conduct a joint venture for developing and marketing a pharmaceutical product, the partnership interests held by the two corporations are not applicable partnership interests.[13]		§ 1061 § 83

D.15. - RECHARACTERIZATION OF CERTAIN GAINS IN THE CASE OF PARTNERSHIP PROFITS INTERESTS HELD IN CONNECTION WITH PERFORMANCE OF INVESTMENT SERVICES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
actually distributed) of partnership items of income and gain, including capital gain eligible for the lower tax rates. A partner's basis in the partnership interest is increased by any amount of gain thus included and is decreased by losses. These basis adjustments prevent double taxation of partnership income to the partner, preserving the partnership's tax status as a passthrough entity. Money distributed to the partner by the partnership is taxed to the extent the amount exceeds the partner's basis in the partnership interest. **<u>Net long-term capital gain</u>** In the case of an individual, estate, or trust, any adjusted net capital gain which otherwise would be taxed at the 10- or 15-percent rate is not taxed. Any adjusted net capital gain which otherwise would be taxed at rates over 15 percent and below 39.6 percent is taxed at a 15-percent rate. Any adjusted net capital gain which otherwise would be taxed at a 39.6-percent rate is taxed at a 20-percent rate. In general, gain or loss reflected in the value of an asset is not recognized for income tax purposes until a taxpayer disposes of the asset. On the sale or exchange of a capital asset, any gain generally is included in income. Short-term capital gain means gain from the sale or exchange of a capital asset held for not more than one year, if and to the extent such gain is taken into account in computing gross income. Net short-term capital loss means the excess of short term capital losses for the taxable year over the short-term capital gains for the taxable year.	**b. Certain Capital Interests.** An applicable partnership interest does not include any capital interest in a partnership giving the taxpayer a right to share in partnership capital commensurate with the amount of capital contributed (as of the time the partnership interest was received), or commensurate with the value of the partnership interest that is taxed under section 83 on receipt or vesting of the partnership interest.[14] For example, in the case of a partner who holds a capital interest in the partnership with respect to capital he or she contributed to the partnership, if the partnership agreement provides that the partner's share of partnership capital is commensurate with the amount of capital he or she contributed (as of the time the partnership interest was received) compared to total partnership capital, the partnership interest is not an applicable partnership interest to that extent.[15] **5. Applicable trade or business.** An applicable trade or business means any activity (regardless of whether the activity are conducted in one or more entities) that consists in whole or in part of the following: (1) raising or returning capital, and either (2) investing in (or disposing of) specified assets (or identifying specified assets for investing or disposition), or (3) developing specified assets.[16] Developing specified assets takes place, for example, if it is represented to investors, lenders, regulators, or others that the value, price, or yield of a portfolio business may be enhanced or increased in		§ 1061 § 83

D.15. - RECHARACTERIZATION OF CERTAIN GAINS IN THE CASE OF PARTNERSHIP PROFITS INTERESTS HELD IN CONNECTION WITH PERFORMANCE OF INVESTMENT SERVICES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Net long-term capital gain means the excess of long-term capital gains for the taxable year over the long-term capital losses for the taxable year. Net capital gain is the excess of the net long-term capital gain for the taxable year over the net short-term capital loss for the year. Gain or loss is treated as long-term if the asset is held for more than one year. The adjusted net capital gain of an individual is the net capital gain reduced (but not below zero) by the sum of the 28-percent rate gain and the unrecaptured section 1250 gain. The net capital gain is reduced by the amount of gain that the individual treats as investment income for purposes of determining the investment interest limitation.	connection with choices or actions of a service provider or of others acting in concert with or at the direction of a service provider.[17] Services performed as an employee of an applicable trade or business are treated as performed in an applicable trade or business for purposes of this rule. Merely voting shares owned does not amount to development; for example, a mutual fund that merely votes proxies received with respect to shares of stock it holds is not engaged in development.[18] 6. **Specified assets.** Under the provision, specified assets means securities (generally as defined under rules for mark-to-market accounting for securities dealers), commodities (as defined under rules for mark-to-market accounting for commodities dealers), real estate held for rental or investment, cash or cash equivalents, options or derivative contracts with respect to such securities, commodities, real estate, cash or cash equivalents, as well as an interest in a partnership the extent of the partnership's proportionate interest in the foregoing.[19] a. **Definition of Security.** A security for this purpose means any (1) share of corporate stock, (2) partnership interest or beneficial ownership interest in a widely held or publicly traded partnership or trust, (3) note, bond, debenture, or other evidence of indebtedness, (4) interest rate, currency, or equity notional principal contract, (5) interest in, or derivative financial instrument in, any such security or any currency (regardless of whether section 1256 applies to		§ 1061 § 83

D.15. - RECHARACTERIZATION OF CERTAIN GAINS IN THE CASE OF PARTNERSHIP PROFITS INTERESTS HELD IN CONNECTION WITH PERFORMANCE OF INVESTMENT SERVICES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	the contract), and (6) position that is not such a security and is a hedge with respect to such a security and is clearly identified. A commodity for this purpose means any (1) commodity that is actively traded, (2) notional principal contract with respect to such a commodity, (3) interest in, or derivative financial instrument in, such a commodity or notional principal contract, or (4) position that is not such a commodity and is a hedge with respect to such a commodity and is clearly identified. For purposes of the provision, real estate held for rental or investment does not include, for example, real estate on which the holder operates an active farm.[20] **b. Partnership Look-Through Rule.** A partnership interest, for purposes of determining the proportionate interest of a partnership in any specified asset, includes any partnership interest that is not otherwise treated as a security for purposes of the provision (for example, an interest in a partnership that is not widely held or publicly traded). For example, assume that a hedge fund acquires an interest in an operating business conducted in the form of a non-publicly traded partnership that is not widely held; the partnership interest is a specified asset for purposes of the provision.[21] **7. Transfer of applicable partnership interest to related person.** If a taxpayer transfers any applicable partnership interest, directly or indirectly, to a person related to the taxpayer, then the taxpayer includes in gross		§ 1061 § 83

D.15. - RECHARACTERIZATION OF CERTAIN GAINS IN THE CASE OF PARTNERSHIP PROFITS INTERESTS HELD IN CONNECTION WITH PERFORMANCE OF INVESTMENT SERVICES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	income as short-term capital gain so much of the taxpayer's net long-term capital gain attributable to the sale or exchange of an asset held for not more than three years as is allocable to the interest.[22] The amount included as short-term capital gain on the transfer is reduced by the amount treated as short-term capital gain on the transfer for the taxable year under the general rule of the provision (that is, amounts are not double-counted).[23] A related person for this purpose is a family member (within the meaning of attribution rules) or colleague, that is a person who performed a service within the current calendar year or the preceding three calendar years in any applicable trade or business in which or for which the taxpayer performed a service.[24] 8. **Reporting requirement.** Treasury is directed to require reporting (at the time in the manner determined by the Secretary) necessary to carry out the purposes of the provision.[25] The penalties otherwise applicable to a failure to report to partners under section 6031(b) apply to failure to report under this requirement.[26] 9. **Regulatory authority.** The Treasury Department is directed to issue regulations or other guidance necessary to carry out the provision. Such guidance is to address prevention of the abuse of the purposes of the provision, including through the allocation of income to tax-indifferent parties.[27] Guidance is also to provide for the application of the provision in the case of tiered structures of entities.[28]		§ 1061 § 83

D.15. - RECHARACTERIZATION OF CERTAIN GAINS IN THE CASE OF PARTNERSHIP PROFITS INTERESTS HELD IN CONNECTION WITH PERFORMANCE OF INVESTMENT SERVICES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	[1] *See* I.R.C. § 1061. [2] I.R.C. § 1061(a). [3] I.R.C. § 1061(a). [4] Conf. Report. [5] I.R.C. § 1061(b). [6] I.R.C. § 1061(c)(5)(A). [7] I.R.C. § 1061(c)(5)(B). [8] I.R.C. § 1061(d)(2). [9] I.R.C. § 1061(c)(1). [10] House Report. [11] I.R.C. § 1061(c)(1). [12] I.R.C. § 1061(c)(4)(A). [13] House Report. [14] I.R.C. § 1061(c)(4)(B). [15] House Report. [16] I.R.C. § 1061(c)(2). [17] House Report. [18] House Report. [19] I.R.C. § 1061(c)(3). [20] I.R.C. § 1061(c)(3). [21] House Report. [22] I.R.C. § 1061(d)(1). [23] I.R.C. § 1061(d)(1). [24] I.R.C. § 1061(d)(2) [25] I.R.C. § 1061(e). [26] House Report. [27] I.R.C. § 1061(f). [28] House Report. [29] Sec. 13309(c)		§ 1061 § 83

D.18 - DENIAL OF DEDUCTION FOR CERTAIN FINES, PENALTIES, AND OTHER AMOUNTS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
The Code denies a deduction for fines or penalties paid to a government for the violation of any law.	1. The provision denies deductibility for any otherwise deductible amount paid or incurred (whether by suit, agreement, or otherwise) to or at the direction of a government or specified nongovernmental entity in relation to the violation of any law or the investigation or inquiry by such government or entity into the potential violation of any law.[1] 2. An exception applies to payments that the taxpayer establishes are either restitution (including remediation of property) or amounts required to come into compliance with any law that was violated or involved in the investigation or inquiry, that are identified in the court order or settlement agreement as restitution, remediation, or required to come into compliance. In the case of any amount of restitution for failure to pay any tax and assessed as restitution under the Code, such restitution is deductible only to the extent it would have been allowed as a deduction if it had been timely paid. The IRS remains free to challenge the characterization of an amount so identified; however, no deduction is allowed unless the identification is made. Restitution or included remediation of property does not include reimbursement of government investigative or litigation costs.[2] 3. The provision applies only where a government (or other entity treated in a manner similar to a government under the provision) is a complainant or investigator with respect to the violation or potential violation of any law. An exception also applies to any amount paid or incurred as taxes due.[3]	The provision denying the deduction and the reporting provision are effective for amounts paid or incurred on or after the date of enactment, except that it would not apply to amounts paid or incurred under any binding order or agreement entered into before such date. Such exception does not apply to an order or agreement requiring court approval unless the approval was obtained before such date.	§ 6050X

D.18 - DENIAL OF DEDUCTION FOR CERTAIN FINES, PENALTIES, AND OTHER AMOUNTS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	The provision requires government agencies (or entities treated as such agencies under the provision) to report to the IRS and to the taxpayer the amount of each settlement agreement or order entered into where the aggregate amount required to be paid or incurred to or at the direction of the government is at least $600 (or such other amount as may be specified by the Secretary of the Treasury as necessary to ensure the efficient administration of the Internal Revenue laws). The report must separately identify any amounts that are for restitution or remediation of property, or correction of noncompliance. The report must be made at the time the agreement is entered into, as determined by the Secretary of the Treasury.[4] [1] I.R.C. §162(f). [2] I.R.C. §162(f)(2). [3] I.R.C. §162(f)(3). [4] **I.R.C. §6050X.**		§ 6050X

D.19. – DENIAL OF DEDUCTION FOR SETTLEMENTS SUBJECT TO NONDISCLOSURE AGREEMENTS PAID IN CONNECTION WITH SEXUAL HARASSMENT OR SEXUAL ABUSE

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
A taxpayer generally is allowed a deduction for ordinary and necessary expenses paid or incurred in carrying on any trade or business. However, certain exceptions apply. No deduction is allowed for (1) any charitable contribution or gift that would be allowable as a deduction under section 170 were it not for the percentage limitations, the dollar limitations, or the requirements as to the time of payment, set forth in such section; (2) any illegal bribe, illegal kickback, or other illegal payment; (3) certain lobbying and political expenditures; (4) any fine or similar penalty paid to a government for the violation of any law; (5) two-thirds of treble damage payments under the antitrust laws; (6) certain foreign advertising expenses; (7) certain amounts paid or incurred by a corporation in connection with the reacquisition of its stock or of the stock of any related person; or (8) certain applicable employee remuneration.	Under the provision, no deduction is allowed for any settlement, payout, or attorney fees related to sexual harassment or sexual abuse if such payments are subject to a nondisclosure agreement.[1] [1] I.R.C. § 162(q). [2] Tax Cuts and Jobs Act § 13307(b).	The provision is effective for amounts paid or incurred after the date of enactment.[2]	§ 162(a)

Tax Reform
Section I

I.1. – MODIFICATION OF LIMITATION ON EXCESSIVE EMPLOYEE REMUNERATION

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
In general An employer generally may deduct reasonable compensation for personal services as an ordinary and necessary business expense. Section 162(m) provides an explicit limitation on the deductibility of compensation expenses in the case of publicly traded corporate employers. The otherwise allowable deduction for compensation with respect to a covered employee of a publicly held corporation is limited to no more than $1 million per year. The deduction limitation applies when the deduction attributable to the compensation would otherwise be taken. **Covered employees** Section 162(m) defines a covered employee as (1) the chief executive officer of the corporation (or an individual acting in such capacity) as of the close of the taxable year and (2) any employee whose total compensation is required to be reported to shareholders under the Securities Exchange Act of 1934 ("Exchange Act") by reason of being among the corporation's four most highly compensated officers for the taxable year (other than the chief executive officer).1008 Treasury regulations under section 162(m) provide that whether an employee is the chief executive officer or among the four most highly compensated officers should be determined pursuant to the executive compensation disclosure rules promulgated under the Exchange Act. In 2006, the Securities and Exchange Commission amended certain rules relating to executive compensation, including which officers' compensation must be disclosed under the Exchange Act. Under the new rules, such officers are (1) the	1. **Definition of covered employee.** The Act revises the definition of covered employee in Section 162(m) to include both the principal executive officer and the principal financial officer.[1] Further, an individual is a covered employee if the individual holds one of these positions at any time during the taxable year.[2] The provision also defines as a covered employee the three (rather than four) most highly compensated officers for the taxable year (other than the principal executive officer or principal financial officer) who are required to be reported on the company's proxy statement (*i.e.*, the statement required pursuant to executive compensation disclosure rules promulgated under the Exchange Act) for the taxable year (or who would be required to be reported on such a statement for a company not required to make such a report to shareholders).[3] This includes such officers of a corporation not required to file a proxy statement but which otherwise falls within the revised definition of a publicly held corporation, as well as such officers of a publicly traded corporation that would otherwise have been required to file a proxy statement for the year (for example, but for the fact that the corporation delisted its securities or underwent a transaction that resulted in the nonapplication of the proxy statement requirement).[4] In addition, if an individual is a covered employee with respect to a corporation for a taxable year beginning after December 31, 2016, the individual remains a covered employee for all future years.[5] Thus, an individual remains a covered employee with respect to compensation otherwise deductible for subsequent years,	The provision is effective for taxable years beginning after December 31, 2017.[11] A transition rule applies to remuneration which is provided pursuant to a written binding contract which was in effect on November 2, 2017 and which was not modified in any material respect on or after such date.[12] The Conference Report states that, for purposes of the transition rule, compensation paid pursuant to a plan qualifies for this exception provided that the right to participate in the plan is part of a written binding contract with the covered employee in effect on November 2, 2017. For example, suppose a covered employee was hired by XYZ Corporation on October 2, 2017 and one of the terms of the written employment contract is that the executive is eligible to participate in the 'XYZ Corporation Executive Deferred Compensation Plan' in accordance with the terms of the plan. Assume further that the terms of the plan provide for participation after 6 months of employment, amounts payable	§ 162(m)

I.1. – MODIFICATION OF LIMITATION ON EXCESSIVE EMPLOYEE REMUNERATION

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
principal executive officer (or an individual acting in such capacity), (2) the principal financial officer (or an individual acting in such capacity), and (3) the three most highly compensated officers, other than the principal executive officer or principal financial officer. In response to the Securities and Exchange Commission's new disclosure rules, the Internal Revenue Service issued updated guidance on identifying which employees are covered by section 162(m). The new guidance provides that "covered employee" means any employee who is (1) as of the close of the taxable year, the principal executive officer (or an individual acting in such capacity) defined in reference to the Exchange Act, or (2) among the three most highly compensated officers for the taxable year (other than the principal executive officer or principal financial officer), again defined by reference to the Exchange Act. Thus, under current guidance, only four employees are covered under section 162(m) for any taxable year. Under Treasury regulations, the requirement that the individual meet the criteria as of the last day of the taxable year applies to both the principal executive officer and the three highest compensated officers. **Definition of publicly held corporation** For purposes of the deduction disallowance of section 162(m), a publicly held corporation means any corporation issuing any class of common equity securities required to be registered under section 12 of the Securities Exchange Act of 1934. All U.S. publicly traded companies are subject to this registration requirement, including their foreign affiliates. A foreign company publicly traded through American depository receipts ("ADRs") is also	including for years during which the individual is no longer employed by the corporation and years after the individual has died.[6] Compensation does not fail to be compensation with respect to a covered employee and thus subject to the deduction limit for a taxable year merely because the compensation is includible in the income of, or paid to, another individual, such as compensation paid to a beneficiary after the employee's death, or to a former spouse pursuant to a domestic relations order.[7] **2. Definition of publicly held corporation.** The provision extends the applicability of section 162(m) to include all domestic publicly traded corporations and all foreign companies publicly traded through ADRs.[8] The proposed definition may include certain additional corporations that are not publicly traded, such as large private C or S corporations.[6] **3. Performance-based compensation and commissions exceptions.** The provision eliminates the exceptions for commissions and performance-based compensation from the definition of compensation subject to the deduction limit. Thus, such compensation is taken into account in determining the amount of compensation with respect to a covered employee for a taxable year that exceeds $1 million and is thus not deductible under section 162.[10]	under the plan are not subject to discretion, and the corporation does not have the right to amend materially the plan or terminate the plan (except on a prospective basis before any services are performed with respect to the applicable period for which such compensation is to be paid). Provided that the other conditions of the binding contract exception are met (e.g., the plan itself is in writing), payments under the plan are grandfathered, even though the employee was not actually a participant in the plan on November 2, 2017.[13] The fact that a plan was in existence on November 2, 2017 is not by itself sufficient to qualify the plan for the exception for binding written contracts.[14] The exception for remuneration paid pursuant to a binding written contract ceases to apply to amounts paid after there has been a material modification to the terms of the contract. The exception does not apply to new contracts entered into or	§ 162(m)

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subject to this registration requirement if more than 50 percent of the issuer's outstanding voting securities are held, directly or indirectly, by residents of United States and either (i) the majority of the executive officers or directors are United States citizens or residents, (ii) more than 50 percent of the assets of the issuer are located in the United States, or (iii) the business of the issuer is administered principally in the United States. Other foreign companies are not subject to the registration requirement. **<u>Remuneration subject to the deduction limitation</u>** **<u>In general</u>** Unless specifically excluded, the deduction limitation applies to all remuneration for services, including cash and the cash value of all remuneration (including benefits) paid in a medium other than cash. If an individual is a covered employee for a taxable year, the deduction limitation applies to all compensation not explicitly excluded from the deduction limitation, regardless of whether the compensation is for services as a covered employee and regardless of when the compensation was earned. The $1 million cap is reduced by excess parachute payments (as defined in section 280G) that are not deductible by the corporation. Certain types of compensation are not subject to the deduction limit and are not taken into account in determining whether other compensation exceeds $1 million. The following types of compensation are not taken into account: (1) remuneration payable on a commission basis; (2) remuneration payable solely on account of the attainment of one or more performance goals if certain outside director and shareholder approval requirements are met		renewed after November 2, 2017. For purposes of this rule, any contract that is entered into on or before November 2, 2017 and that is renewed after such date is treated as a new contract entered into on the day the renewal takes effect. A contract that is terminable or cancelable unconditionally at will by either party to the contract without the consent of the other, or by both parties to the contract, is treated as a new contract entered into on the date any such termination or cancellation, if made, would be effective. However, a contract is not treated as so terminable or cancelable if it can be terminated or cancelled only by terminating the employment relationship of the covered employee.	§ 162(m)

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("performance-based compensation"); (3) payments to a tax-favored retirement plan (including salary reduction contributions); (4) amounts that are excludable from the executive's gross income (such as employer-provided health benefits and miscellaneous fringe benefits); and (5) any remuneration payable under a written binding contract which was in effect on February 17, 1993. In addition, remuneration does not include compensation for which a deduction is allowable after a covered employee ceases to be a covered employee. Thus, the deduction limitation often does not apply to deferred compensation that is otherwise subject to the deduction limitation (*e.g.*, is not performance-based compensation) because the payment of compensation is deferred until after termination of employment. **<u>Performance-based compensation</u>** Compensation qualifies for the exception for performance-based compensation only if (1) it is paid solely on account of the attainment of one or more performance goals, (2) the performance goals are established by a compensation committee consisting solely of two or more outside directors, (3) the material terms under which the compensation is to be paid, including the performance goals, are disclosed to and approved by the shareholders in a separate majority- approved vote prior to payment, and (4) prior to payment, the compensation committee certifies that the performance goals and any other material terms were in fact satisfied. Compensation (other than stock options or other stock appreciation rights ("SARs")) is not treated as paid solely on account of the attainment of one or more performance goals unless the compensation is			§ 162(m)

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paid to the particular executive pursuant to a pre-established objective performance formula or standard that precludes discretion. A stock option or SAR with an exercise price not less than the fair market value, on the date the option or SAR is granted, of the stock subject to the option or SAR, generally is treated as meeting the exception for performance-based compensation, provided that the requirements for outside director and shareholder approval are met (without the need for certification that the performance standards have been met). This is the case because the amount of compensation attributable to the options or SARs received by the executive is based solely on an increase in the corporation's stock price. Stock-based compensation is not treated as performance-based if it depends on factors other than corporate performance.	[1] I.R.C. § 162(m)(3)(A). [2] I.R.C. 162(m)(3)(A). [3] I.R.C. § 162(m)(3)(B). [4] I.R.C. § 162(m)(3); House Report. [5] I.R.C. § 162(m)(3)(C). [6] House Report. [7] I.R.C. § 162(m)(4)(F); House Report. [8] I.R.C. § 162(m)(2); House Report. [9] House Report. [10] Act Sec. 13601(a)(1). [11] Act Sec. 13601(e)(1). [12] Act Sec. 13601(e)(2). [13] Conf. Report. [14] Conf. Report.		§ 162(m)

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Taxable employers and other service recipients generally may deduct reasonable compensation expenses. However, in some cases, compensation in excess of specific levels is not deductible. A publicly held corporation generally cannot deduct more than $1 million of compensation (that is not compensation otherwise excepted from this limit) in a taxable year for each "covered employee." For this purpose, a covered employee is the corporation's principal executive officer (or an individual acting in such capacity) defined in reference to the Securities Exchange Act of 1934 ("Exchange Act") as of the close of the taxable year, or any employee whose total compensation is required to be reported to shareholders under the Exchange Act by reason of being among the corporation's three most highly compensated officers for the taxable year (other than the principal executive officer or principal financial officer). Unless an exception applies, generally a corporation cannot deduct that portion of the aggregate present value of a "parachute payment" which equals or exceeds three times the "base amount" of certain service providers. The nondeductible excess is an "excess parachute payment." A parachute payment is generally a payment of compensation that is contingent on a change in corporate ownership or control made to certain officers, shareholders, and highly compensated individuals. An individual's base amount is the average annualized compensation includible in the individual's gross income for the five taxable years ending before the date on which the change in ownership or control occurs. Certain amounts are not considered parachute payments,	**1. 21% Excise Tax.** Under the provision, an employer is liable for an excise tax equal to 21% of the sum of (1) any remuneration (other than an excess parachute payment) in excess of $1 million paid to a covered employee by an applicable tax-exempt organization for a taxable year;[1] and (1) any excess parachute payment (under a new definition for this purpose that relates solely to separation pay) paid by the applicable tax-exempt organization to a covered employee.[2] Accordingly, the excise tax applies as a result of an excess parachute payment, even if the covered employee's remuneration does not exceed $1 million.[3] Remuneration is treated as paid when there is no substantial risk of forfeiture of the rights to such remuneration.[4] "Substantial risk of forfeiture" is based on the definition in 457(f)(3)(B) which applies to ineligible deferred compensation subject to section 457(f).[5] Accordingly, the Conference Report states that the tax imposed by this provision can apply to the value of remuneration that is vested (and any increases in such value or vested remuneration) under this definition, even if it is not yet received.[6] **2. Covered Employee.** A covered employee is an employee (including any former employee) of an applicable tax-exempt organization if the employee is one of the five highest compensated employees of the organization for the taxable year or was a covered employee of the organization (or a predecessor) for any preceding taxable year beginning after December 31, 2016.[7] An "applicable tax-exempt organization" is an organization exempt from tax under section 501(a), an exempt farmers' cooperative, a Federal, State or local governmental entity with excludable income, or a political organization.[8]	The provision is effective for taxable years beginning after December 31, 2017.[22]	§ 4960

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including payments under a qualified retirement plan, a simplified employee pension plan, or a simple retirement account. These deduction limits generally do not affect a tax-exempt organization.	**3. Remuneration.** **a. In General.** Remuneration means wages as defined for income tax withholding purposes, but does not include any designated Roth contribution and includes amounts required to be included in gross income.[9] The term "remuneration" does not include the portion of any remuneration paid to a licensed medical professional (including a veterinarian) which is for the performance of medical or veterinary services by such professional.[10] **b. Remuneration from Related Organizations.** Remuneration of a covered employee includes any remuneration paid with respect to employment of the covered employee by any person or governmental entity related to the applicable tax-exempt organization.[11] A person or governmental entity is treated as related to an applicable tax-exempt organization if the person or governmental entity (1) controls, or is controlled by, the organization, (2) is controlled by one or more persons that control the organization, (3) is a supported organization during the taxable year with respect to the organization, (4) is a supporting organization during the taxable year with respect to the organization, or (5) in the case of a voluntary employees' beneficiary association ("VEBA"), establishes, maintains, or makes contributions to the VEBA.[12] However, remuneration of a covered employee that is not deductible by reason of the $1 million limit on deductible compensation is not taken into account for purposes of the provision.[13]		§ 4960

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	4. Excess Parachute Payment. An excess parachute payment is the amount by which any parachute payment exceeds the portion of the base amount allocated to the payment.[14] A parachute payment is a payment in the nature of compensation to (or for the benefit of) a covered employee if the payment is contingent on the employee's separation from employment and the aggregate present value of all such payments equals or exceeds three times the base amount.[15] The base amount is the average annualized compensation includible in the covered employee's gross income for the five taxable years ending before the date of the employee's separation from employment.[16] Parachute payments do not include (1) any payment under a qualified retirement plan, under a simplified employee pension plan, a simple retirement account, a tax-deferred annuity, or an eligible deferred compensation plan of a State or local government employer;[17] (2) a payment to an licensed medical professional (including a veterinarian) to the extent that such payment is for the performance of medical or veterinary services by such professional;[18] or (3) a payment to an individual who is not a highly compensated employee as defined in Section 414(q).[19] **5. Liability for Tax.** The employer of a covered employee is liable for the excise tax.[20] If remuneration of a covered employee from more than one employer is taken into account in determining the excise tax, each employer is liable for the tax in an amount that bears the same ratio to the total tax as the remuneration paid by that employer bears to the remuneration paid by all employers to the covered employee.[21]		§ 4960

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	[1] I.R.C. § 4960(a)(1). [2] I.R.C. § 4960(a)(2). [3] House Report. [4] I.R.C. § 4960(a)(1). [5] I.R.C. § 4960(a). [6] Conf. Report. [7] I.R.C. § 4960(c)(2). [8] I.R.C. § 4960(c)(1). [9] I.R.C. § 4960(c)(3). [10] I.R.C. § 4960(c)(3)(B). [11] I.R.C. § 4960A(c)(4)(A). [12] I.R.C. § 4960(c)(4)(B). [13] I.R.C. § 4960(c)(6); House Report [14] I.R.C. § 4960(c)(5)(A). [15] I.R.C. § 4960(c)(5)(B). [16] I.R.C. § 4960(c)(5)(D); *see* I.R.C. § 280G(b)(3). [17] I.R.C. § 4960(c)(5)(C). [18] I.R.C. § 4960(c)(5)(C)(iii). [19] I.R.C. § 4960(c)(5)(C)(iv). [20] I.R.C. § 4960(b). [21] I.R.C. § 4960(c)(4)(C). [22] Act Sec. 13602(c).		§ 4960

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<u>Income tax treatment of employer stock transferred to an employee</u> Specific rules apply to property, including employer stock, transferred to an employee in connection with the performance of services. These rules govern the amount and timing of income inclusion by the employee and the amount and timing of the employer's compensation deduction. Under these rules, an employee generally must recognize income in the taxable year in which the employee's right to the stock is transferable or is not subject to a substantial risk of forfeiture, whichever occurs earlier (referred to herein as "substantially vested"). Thus, if the employee's right to the stock is substantially vested when the stock is transferred to the employee, the employee recognizes income in the taxable year of such transfer, in an amount equal to the fair market value of the stock as of the date of transfer (less any amount paid for the stock). If at the time the stock is transferred to the employee, the employee's right to the stock is not substantially vested (referred to herein as "nonvested"), the employee does not recognize income attributable to the stock transfer until the taxable year in which the employee's right becomes substantially vested. In this case, the amount includible in the employee's income is the fair market value of the stock as of the date that the employee's right to the stock is substantially vested (less any amount paid for the stock). However, if the employee's right to the stock is nonvested at the time the stock is transferred to employee, under section 83(b), the employee may elect within 30 days of transfer to recognize income in the taxable year of transfer, referred to as a "section 83(b)" election. If a proper and timely	**A. Election to Defer Inclusion.** **1. General Rule.** The provision allows a qualified employee to elect to defer, for income tax purposes, the inclusion in income of the amount of income attributable to qualified stock transferred to the employee by the employer.[1] **2. Exceptions.** No election may be made with respect to any qualified stock if: a. The qualified employee has made an election under Section 83(b) with respect to such stock.[2] Section 83(i)(7) provides that "[t]his section (other than this subsection), including any election under subsection (b), shall not apply to restricted stock units." The provision clarifies that Section 83 (other than the election provision), including Section 83 (b), does not apply to RSUs. Therefore, RSUs are not eligible for a section 83(b) election. According to the House Report, this is the case because, absent this provision, RSUs are nonqualified deferred compensation and therefore subject to the rules that apply to nonqualified deferred compensation.[3] b. Any stock of the corporation which issued the qualified stock is readily tradable on an established securities market (as determined under) at any time before the election is made.[4] c. If, in the preceding calendar year, the corporation purchased any of its outstanding stock unless at least 25 percent of the total dollar amount of the stock so purchased is stock with respect to which an inclusion deferral election is in effect ("deferral stock"[5]) and the determination of which individuals from whom deferral stock is purchased is made on a reasonable basis.[6] For	The provision generally applies with respect to stock attributable to options exercised or RSUs settled after December 31, 2017.[48] Under a transition rule, until the Secretary (or the Secretary's delegate) issues regulations or other guidance implementing the 80-percent and employer notice requirements under the provision, a corporation will be treated as complying with those requirements (respectively) if it complies with a reasonable good faith interpretation of the requirements.[49] The penalty for a failure to provide the notice required under the provision applies to failures after December 31, 2017.	§ 83 § 3401 § 6051

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election under section 83(b) is made, the amount of compensatory income is capped at the amount equal to the fair market value of the stock as of the date of transfer (less any amount paid for the stock). A section 83(b) election is available with respect to grants of "restricted stock" (nonvested stock), and does not generally apply to the grant of options. In general, an employee's right to stock or other property is subject to a substantial risk of forfeiture if the employee's right to full enjoyment of the property is subject to a condition, such as the future performance of substantial services. An employee's right to stock or other property is transferable if the employee can transfer an interest in the property to any person other than the transferor of the property. Thus, generally, employer stock transferred to an employee by an employer is not transferable merely because the employee can sell it back to the employer. In the case of stock transferred to an employee, the employer is allowed a deduction (to the extent a deduction for a business expense is otherwise allowable) equal to the amount included in the employee's income as a result of transfer of the stock. The employer deduction generally is permitted in the employer's taxable year in which or with which ends the employee's taxable year when the amount is included and properly reported in the employee's income. These rules do not apply to the grant of a nonqualified option on employer stock unless the option has a readily ascertainable fair market value. Instead, these rules apply to the transfer of employer stock by the employee on exercise of the option. That is, if the right to the stock is substantially vested	purposes of this requirement, stock purchased from an individual is not treated as deferral stock (and the purchase is not treated as a purchase of deferral stock) if, immediately after the purchase, the individual holds any deferral stock with respect to which an inclusion deferral election has been in effect for a longer period than the election with respect to the purchased stock.[7] Thus, in general, in applying the purchase requirement, an individual's deferral stock with respect to which an inclusion deferral election has been in effect for the longest periods must be purchased first.[8] A corporation that has deferral stock outstanding as of the beginning of any calendar year and that purchases any of its outstanding stock during the calendar year must report on its income tax return for the taxable year in which, or with which, the calendar year ends the total dollar amount of the outstanding stock purchased during the calendar year and such other information as Treasury may require for purposes of administering this requirement.[9] **B. Time and Manner for Making Election.** **1. Time.** An election to defer income inclusion ("inclusion deferral election") with respect to qualified stock must be made no later than 30 days after the first date the employee's right to the stock is transferable or not subject to a substantial risk of forfeiture, whichever occurs earlier.[10] **2. Manner.** An inclusion deferral election is made in a manner similar to the manner in which a section 83(b) election is made.[11] Thus, the House Report notes that, as in the case of a section 83(b) election under present law, the employee must file with the IRS the inclusion deferral election and provide the employer with a copy.[12]		§ 83 § 3401 § 6051

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on transfer (the time of exercise), income recognition applies for the taxable year of transfer. If the right to the stock is nonvested on transfer, the timing of income inclusion is determined under the rules applicable to the transfer of nonvested stock. In either case, the amount includible in income by the employee is the fair market value of the stock as of the required time of income inclusion, less the exercise price paid by the employee. A section 83(b) election generally does not apply to the grant of options. If upon the exercise of an option, nonvested stock is transferred to the employee, a section 83(b) election may apply. The employer's deduction is generally determined under the rules that apply to transfers of restricted stock, but a special accrual rule may apply under Treasury regulations when the transferred stock is substantially vested. **<u>Employment taxes and reporting</u>** Employment taxes generally consist of taxes under the Federal Insurance Contributions Act ("FICA"), tax under the Federal Unemployment Tax Act ("FUTA"), and income taxes required to be withheld by employers from wages paid to employees ("income tax withholding"). Unless an exception applies under the applicable rules, compensation provided to an employee constitutes wages subject to these taxes. FICA imposes tax on employers and employees, generally based on the amount of wages paid to an employee during the year. Special rules as to the timing and amount of FICA taxes apply in the case of nonqualified deferred compensation, as defined for FICA purposes.	**3. Revocation.** The statute provides that an inclusion deferral election is revoked at the time and in the manner as the Secretary provides.[13] **C. Taxable Year of Inclusion and Taxable Year of Deduction for Employer.** **1. Taxable Year of Inclusion.** If an employee elects to defer income inclusion under the provision, the income must be included in the employee's income for the taxable year that includes the earliest of: a. The first date the qualified stock becomes transferable, including, solely for this purpose, transferable to the employer;[14] b. The date the employee first becomes an excluded employee (as described below);[15] c. The first date on which any stock of the employer becomes readily tradable on an established securities market;[16] d. The date five years after the first date the employee's right to the stock are transferable or not subject to a substantial risk of forfeiture;[17] or e. The date on which the employee revokes her inclusion deferral election.[18] **2. Taxable Year of Deduction for Employer.** Deferred income inclusion applies also for purposes of the employer's deduction of the amount of income attributable to the qualified stock. That is, if an employee makes an inclusion deferral election, the employer's deduction is deferred until the employer's taxable year in		§ 83 § 3401 § 6051

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The tax imposed on the employer and on the employee is each composed of two parts: (1) the Social Security or old age, survivors, and disability insurance ("OASDI") tax equal to 6.2 percent of covered wages up to the OASDI wage base ($127,200 for 2017); and (2) the Medicare or hospital insurance ("HI") tax equal to 1.45 percent of all covered wages. The employee portion of FICA tax generally must be withheld and, along with the employer portion, remitted to the Federal government by the employer. FICA tax withholding applies regardless of whether compensation is provided in the form of cash or a noncash form, such as a transfer of property (including employer stock) or in-kind benefits. FUTA imposes a tax on employers of six percent of wages up to the FUTA wage base of $7,000. Income tax withholding generally applies when wages are paid by an employer to an employee, based on graduated withholding rates set out in tables published by the Internal Revenue Service ("IRS"). Like FICA tax withholding, income tax withholding applies regardless of whether compensation is provided in the form of cash or a noncash form, such as a transfer of property (including employer stock) or in-kind benefits. An employer is required to furnish each employee with a statement of compensation information for a calendar year, including taxable compensation, FICA wages, and withheld income and FICA taxes. In addition, information relating to certain nontaxable items must be reported, such as certain retirement and health plan contributions. The statement, made on Form W-2, Wage and Tax Statement, must be provided to each employee by January 31 of the succeeding year.	which or with which ends the taxable year of the employee for which the amount is included in the employee's income as described in a through e above.[19] **D. Treatment of Qualified Stock Attributable to Statutory Option.** A qualified employee may make an inclusion deferral election with respect to qualified stock attributable to a statutory option.[20] In that case, the option is not treated as a statutory option and the rules relating to statutory options and related stock do not apply.[21] In addition, an arrangement under which an employee may receive qualified stock is not treated as a nonqualified deferred compensation plan solely because of an employee's inclusion deferral election or ability to make an election.[22] The conference report clarifies that (1) when an inclusion deferral election is made with respect to stock transferred under an ESPP, the option is not considered an ESPP, such that when an inclusion deferral election is made in connection with the exercise of both ESPPs and ISOs, the options are not treated as statutory options but rather as nonqualified stock options for FICA purposes (in addition to being subject to section 83(i) for income tax purposes).[23] **E. Qualified employee and qualified stock.** **1. Qualified Employee.** A qualified employee means an individual who is not an excluded employee and who agrees, in the inclusion deferral election, to meet the requirements necessary (as determined by the Secretary) to ensure the income tax withholding requirements of the employer corporation with respect to the qualified stock (as described		§ 83 § 3401 § 6051

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Statutory options Two types of statutory options apply with respect to employer stock: incentive stock options ("ISOs") and options provided under an employee stock purchase plan ("ESPP"). Stock received pursuant to a statutory option is subject to special rules, rather than the rules for nonqualified options, discussed above. No amount is includible in an employee's income on the grant, vesting, or exercise of a statutory option. In addition, generally no deduction is allowed to the employer with respect to the option or the stock transferred to an employee. If a holding requirement is met with respect to the stock transferred on exercise of a statutory option and the employee later disposes of the stock, the employee's gain generally is treated as capital gain rather than ordinary income. Under the holding requirement, the employee must not dispose of the stock within two years after the date the option is granted and also must not dispose of the stock within one year after the date the option is exercised. If a disposition occurs before the end of the required holding period (a "disqualifying disposition"), the employee recognizes ordinary income in the taxable year in which the disqualifying disposition occurs and the employer may be allowed a corresponding deduction in the taxable year in which such disposition occurs. The amount of ordinary income recognized when a disqualifying disposition occurs generally equals the fair market value of the stock on the date of exercise (that is, when the stock was transferred to the employee) less the exercise price paid.	below) are met.[24] For this purpose, an excluded employee with respect to a corporation is any individual (1) who was a one-percent owner of the corporation[25] at any time during the calendar year or who was such a 1 percent owner at any time during the 10 preceding calendar years;[26] (2) who is, or has been at any prior time, the chief executive officer or chief financial officer of the corporation or an individual acting in either capacity;[27] (3) who is a family member of an individual described in (1) or (2);[28] or (4) who has been one of the four highest compensated officers of the corporation for any of the 10 preceding taxable years, determined on the basis of shareholder disclosure rules for compensation under the Securities Exchange Act of 1934, as if such rules applied to the corporation.[29] **2. Qualified Stock.** Qualified stock is any stock of a corporation if (1) an employee receives the stock in connection with the exercise of an option or in settlement of an RSU, and (2) the option or RSU was granted by the corporation to the employee in connection with the performance of services and in a year in which the corporation was an eligible corporation (as described below).[30] However, qualified stock does not include any stock if, at the time the employee's right to the stock becomes substantially vested, the employee may sell the stock to, or otherwise receive cash in lieu of stock from, the corporation.[31] Qualified stock can only be such if it relates to stock received in connection with options or RSUs, and does not include stock received in connection with other forms of equity compensation, including stock appreciation rights or restricted stock.[32]		§ 83 § 3401 § 6051

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Employment taxes do not apply with respect to the grant or vesting of a statutory option, transfer of stock pursuant to the option, or a disposition (including a disqualifying disposition) of the stock. However, certain special reporting requirements apply. **<u>Nonqualified deferred compensation</u>** Compensation is generally includible in an employee's income when paid to the employee. However, in the case of a nonqualified deferred compensation plan, unless the arrangement either is exempt from or meets the requirements of section 409A, the amount of deferred compensation is first includible in income for the taxable year when not subject to a substantial risk of forfeiture (as defined), even if payment will not occur until a later year. In general, to meet the requirements of section 409A, the time when nonqualified deferred compensation will be paid, as well as the amount, must be specified at the time of deferral with limits on further deferral after the time for payment. Various other requirements apply, including that payment can only occur on specific defined events. Various exemptions from section 409A apply, including transfers of property subject to section 83.1058 Nonqualified options are not automatically exempt from section 409A, but may be structured so as not to be considered nonqualified deferred compensation. A restricted stock unit ("RSU") is a term used for an arrangement under which an employee has the right to receive at a specified time in the future an amount determined by reference to the value of one or more shares of employer stock. An employee's right to receive the future amount may be subject to a condition, such as continued	**3. Eligible Corporation.** A corporation is an eligible corporation with respect to a calendar year if (1) no stock of the employer corporation (or any predecessor) is readily tradable on an established securities market during any preceding calendar year,[33] and (2) the corporation has a written plan under which, in the calendar year, not less than 80 percent of all employees who provide services to the corporation in the United States (or any U.S. possession) are granted stock options, or are granted restricted stock units ("RSUs"), with the same rights and privileges to receive qualified stock ("80-percent requirement").[34] For this purpose, in general, the determination of rights and privileges with respect to stock is determined in a similar manner as provided under the present-law ESPP rules.[35] Employees, however, will not fail to be treated as having the same rights and privileges to receive qualified stock solely because the number of shares available to all employees is not equal in amount, provided that the number of shares available to each employee is more than a de minimis amount.[36] In addition, rights and privileges with respect to the exercise of a stock option are not treated for this purpose as the same as rights and privileges with respect to the settlement of an RSU. I.R.C. Sec. 83(i)(2)(C)(ii)(III). Under a transition rule, in the case of a calendar year beginning before January 1, 2018, the 80-percent requirement is applied without regard to whether the rights and privileges with respect to the qualified stock are the same. I.R.C. Sec. 83(i)(2)(C)(iv). For purposes of the requirement that an ESPP provide employees with the same rights and		§ 83 § 3401 § 6051

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Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
employment for a certain period or the attainment of certain performance goals. The payment to the employee of the amount due under the arrangement is referred to as settlement of the RSU. The arrangement may provide for the settlement amount to be paid in cash or as a transfer of employer stock (or either). An arrangement providing RSUs is generally considered a nonqualified deferred compensation plan and is subject to the rules, including the limits, of section 409A. The employer deduction generally is permitted in the employer's taxable year in which or with which ends the employee's taxable year when the amount is included and properly reported in the employee's income.	privileges, the rules of the provision apply in determining which employees have the right to make an inclusion deferral election with respect to stock received under the ESPP.[37] **F. Controlled Groups.** For purposes of the provision, corporations that are members of the same controlled group are treated as one corporation.[38] **G. Notice, withholding and reporting requirements.** A corporation that transfers qualified stock to a qualified employee must provide a notice to the qualified employee at the time (or a reasonable period before) an amount would first be includible absent an inclusion deferral election).[39] The notice must certify to the employee that the stock is qualified stock, and notify the employee (a) that the employee may (if eligible) elect to defer income inclusion with respect to the stock and (b) that, if the employee makes an inclusion deferral election: (1) the amount of income required to be included at the end of the deferral period will be based on the value of the stock at the time the employee's right to the stock first becomes substantially vested, notwithstanding whether the value of the stock has declined during the deferral period (including whether the value of the stock has declined below the employee's tax liability with respect to such stock); (2) the amount of income to be included at the end of the deferral period will be subject to withholding as provided under the provision; and (3) the employee's responsibilities with respect to required withholding.[40] Failure to provide the notice may result in the imposition of a penalty of $100 for each failure, subject to a maximum penalty of $50,000 for all failures during any calendar year.[41]		§ 83 § 3401 § 6051

I.3. – TREATMENT OF QUALIFIED EQUITY GRANTS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	H. Income Tax Withholding and Reporting. **1. Withholding.** An inclusion deferral election applies only for income tax purposes.[42] The application of FICA and FUTA are not affected.[43] The provision includes specific income tax withholding and reporting requirements with respect to income subject to an inclusion deferral election.[44] For purposes of the determination of wages for income tax withholding, qualified stock with respect to which an deferral election is made under section 83(i) is treated as wages (1) received on the earliest date described in Section 83(i)(1)(B), and (2) in an amount equal to the amount included in income under Section 83 for the taxable year which includes such date.[45] **2. Reporting.** For the taxable year for which income subject to an inclusion deferral election is required to be included in income by the employee (as described above), the amount required to be included in income is treated as wages with respect to which the employer is required to withhold income tax at a rate not less than the highest income tax rate applicable to individual taxpayers.[46] The employer must report on Form W-2 the amount of income covered by an inclusion deferral election (1) for the year of deferral; and (2) for the year the income is required to be included in income by the employee. In addition, for any calendar year, the employer must report on Form W-2 the aggregate amount of income covered by inclusion deferral elections, determined as of the close of the calendar year.[47]		§ 83 § 3401 § 6051

I.3. – TREATMENT OF QUALIFIED EQUITY GRANTS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	[1] I.R.C. § 83(i)(1)(A). [2] I.R.C. § 83(i)(4)(B)(i). [3] House Report. [4] Act Sec. 83(i)(4)(B)(ii). [5] I.R.C. § 83(i)(4)(C)(i). [6] This requirement is met if the stock purchased by the corporation includes all the corporation's outstanding deferral stock. *See* I.R.C. § 83(i)(4)(C)(iii). House Report. [7] I.R.C. § 83(i)(4)(C)(ii). [8] House Report. [9] I.R.C. § 83(i)(4)(C)(iv). [10] I.R.C. § 83(i)(4)(A). [11] I.R.C. § 83(i)(4)(A). [12] House Report. [13] I.R.C. § 83(i)(1)(B)(v). [14] I.R.C. § 83(i)(1)(B)(i). Thus, for this purpose, the qualified stock is considered transferable if the employee has the ability to sell the stock to the employer (or any other person). House Report. [15] I.R.C. § 83(i)(1)(B)(ii). [16] I.R.C. § 83(i)(1)(B)(iii). [17] I.R.C. § 83(i)(1)(B)(iv). [18] I.R.C. § 83(i)(1)(B)(v). [19] I.R.C. § 83(h); House Report. [20] *See* I.R.C. § 422(b). [21] I.R.C. § 422(b). [22] I.R.C. § 409A(d)(7). [23] I.R.C. § 423(d). [24] I.R.C. § 83(i)(3). [25] One-percent owner status is determined under the top-heavy rules for qualified retirement plans, that is, section 416(i)(1)(B)(ii). I.R.C. § 83(i)(3)(B)(i). [26] I.R.C. § 83(i)(3)(B)(i).		§ 83 § 3401 § 6051

I.3. – TREATMENT OF QUALIFIED EQUITY GRANTS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	[27] I.R.C. § 83(i)(3)(B)(ii). [28] I.R.C. § 83(i)(3)(B)(iii). [29] I.R.C. § 83(i)(3)(B)(iv). [30] I.R.C. § 83(i)(2)(A). [31] I.R.C. § 83(i)(2)(B). [32] House Report. [33] This requirement continues to apply up to the time an inclusion deferral election is made. That is, under the provision, no inclusion deferral election may be made with respect to qualified stock if any stock of the corporation is readily tradable on an established securities market at any time before the election is made. House Report. [34] I.R.C. § 83(i)(2)(C)(i)(II). In applying the requirement that 80 percent of employees receive stock options or RSUs, excluded employees and part-time employees are not taken into account. I.R.C. § 83(i)(2)(C)(iii). For this purpose, part-time employee is defined under section 4980G(d)(4), as an employee who is customarily employed for fewer than 30 hours per week. The Conference Report clarifies that the requirement that 80 percent of all applicable employees be granted stock options or restricted stock units with the same rights and privileges cannot be satisfied in a taxable year by granting a combination of stock options and RSUs, and instead all such employees must either be granted stock options or be granted restricted stock units for that year. Conf. Report. The Conf. Report also provides that it is intended that the requirement that 80 percent of all applicable employees be granted stock options or be granted restricted stock units apply consistently to eligible employees, whether they are new hires or existing employees. Conf. Report.		§ 83 § 3401 § 6051

I.3. – TREATMENT OF QUALIFIED EQUITY GRANTS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	[35] I.R.C. § 83(i)(2)(C)(ii)(I); *see* I.R.C. § 423(b)(5). [36] I.R.C. § 83(i)(2)(C)(ii)(II). [37] I.R.C. § 423(b)(5). [38] I.R.C. § 83(i)(5). [39] I.R.C. § 83(i)(6). [40] I.R.C. § 83(i)(6). [41] I.R.C. § 6652(p). [42] House Report. [43] House Report. [44] *See* I.R.C. § 3401(i). [45] I.R.C. § 3401(i). [46] I.R.C. § 6051(a)(16); I.R.C. § 3402(t). [47] I.R.C. § 6051(a)(17). [48] Act Sec. 13603(f)(1). [49] I.R.C. § 13603(g).		§ 83 § 3401 § 6051

Tax Reform
Section J

J.1. - TREATMENT OF GAIN OR LOSS OF FOREIGN PERSONS FROM SALE OR EXCHANGE OF INTERESTS IN PARTNERSHIPS ENGAGED IN TRADE OR BUSINESS WITHIN THE US

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
In general A partnership generally is not treated as a taxable entity, but rather, income of the partnership is taken into account on the tax returns of the partners. The character (as capital or ordinary) of partnership items passes through to the partners as if the items were realized directly by the partners. A partner holding a partnership interest includes in income its distributive share (whether or not actually distributed) of partnership items of income and gain, including capital gain eligible for the lower tax rates, and deducts its distributive share of partnership items of deduction and loss. A partner's basis in the partnership interest is increased by any amount of gain and decreased by ay amount of losses thus included. These basis adjustments prevent double taxation of partnership income to the partner. Money distributed to the partner by the partnership is taxed to the extent the amount exceeds the partner's basis in the partnership interest. Gain or loss from the sale or exchange of a partnership interest generally is treated as gain or loss from the sale or exchange of a capital asset. However, the amount of money and the fair market value of property received in the exchange that represent the partner's share of certain ordinary income-producing assets of the partnership give rise to ordinary income rather than capital gain. In general, a partnership does not adjust the basis of partnership property following the transfer of a partnership interest unless either the partnership has made a one-time election to do so, or the partnership has a substantial built-in loss immediately after the transfer. If an election is in effect or the partnership	1. **In General.** Under the provision, gain or loss from the sale or exchange of an interest in a partnership, which is engaged in a U.S. trade or business, is effectively connected with the partnership's U.S. trade or business to the extent that the transferor would have had effectively connected gain or loss had the partnership sold all of its assets at fair market value as of the date of the sale or exchange.[1] The provision requires that in determining the amount of effectively connected gain or loss from the deemed asset sale by the partnership, distributions of such hypothetical gain or loss should be allocated in the same manner as nonseparately stated income and loss.[2] 2. **Withholding Requirements.** The provision requires the transferee of a partnership interest to withhold 10 percent of the amount realized on the sale or exchange of a partnership interest if any portion of the resulting gain (if any) is treated as effectively connected with the partnership's U.S. trade or business under Section 864(c)(8).[3] The provision applies unless the transferor delivers an affidavit to the transferee that the transferor is not a foreign person.[4] If the transferee fails to withhold the correct amount, the partnership is required to deduct and withhold from distributions to the transferee partner an amount equal to the amount the transferee failed to withhold (plus interest).[5]	The portion of the provision treating gain or loss on sale of a partnership interest as effectively connected income is effective for sales, exchanges, and dispositions on or after November 27, 2017.[8] The portion of the provision requiring withholding on sales or exchanges of partnership interests is effective for sales, exchanges, and dispositions after December 31, 2017.[9]	§ 864(c) § 1446

J.1. - TREATMENT OF GAIN OR LOSS OF FOREIGN PERSONS FROM SALE OR EXCHANGE OF INTERESTS IN PARTNERSHIPS ENGAGED IN TRADE OR BUSINESS WITHIN THE US

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
has a substantial built-in loss immediately after the transfer, adjustments are made with respect to the transferee partner. These adjustments are to account for the difference between the transferee partner's proportionate share of the adjusted basis of the partnership property and the transferee partner's basis in its partnership interest. The effect of the adjustments on the basis of partnership property is to approximate the result of a direct purchase of the property by the transferee partner. **<u>Source of gain or loss on transfer of a partnership interest</u>** A foreign person that is engaged in a trade or business in the United States is taxed on income that is "effectively connected" with the conduct of that trade or business ("effectively connected gain or loss"). Partners in a partnership are treated as engaged in the conduct of a trade or business within the United States if the partnership is so engaged. Any gross income derived by the foreign person that is not effectively connected with the person's U.S. business is not taken into account in determining the rates of U.S. tax applicable to the person's income from the business.	**3. Treasury Regulations.** The provision provides the Secretary of the Treasury with specific regulatory authority to address the following: **a. Coordination with Nonrecognition Provisions.** The provision directs the Secretary to issue such regulations as the Secretary determines appropriate for the application of the paragraph, including in exchanges described in sections 332, 351, 354, 355, 356, or 361.[6] **b. Withholding Requirements Guidance.** The provision directs the Secretary to provide regulations and other guidance necessary to carry out the withholding requirements outlined above.[7]	The portion of the provision treating gain or loss on sale of a partnership interest as effectively connected income is effective for sales, exchanges, and dispositions on or after November 27, 2017.[8] The portion of the provision requiring withholding on sales or exchanges of partnership interests is effective for sales, exchanges, and dispositions after December 31, 2017.[9]	§ 864(c) § 1446

1 I.R.C. § 864(c)(8)(A), (B).
2 I.R.C. § 864(B) (flush language).
3 I.R.C. § 1446(f)(1).
4 I.R.C. § 1446(f)(2)(A); *see* I.R.C. § 1446(f)(5), 1445(f)(3) (defining "foreign person" for purposes of I.R.C. § 1446(f)).
5 I.R.C. § 1446(f)(4).
6 I.R.C. § 864(c)(8)(E).

J.1. - TREATMENT OF GAIN OR LOSS OF FOREIGN PERSONS FROM SALE OR EXCHANGE OF INTERESTS IN PARTNERSHIPS ENGAGED IN TRADE OR BUSINESS WITHIN THE US

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Among the factors taken into account in determining whether income, gain, or loss is effectively connected gain or loss are the extent to which the income, gain, or loss is derived from assets used in or held for use in the conduct of the U.S. trade or business and whether the activities of the trade or business were a material factor in the realization of the income, gain, or loss (the "asset use" and "business activities" tests). In determining whether the asset use or business activities tests are met, due regard is given to whether such assets or such income, gain, or loss were accounted for through such trade or business. Thus, notwithstanding the general rule that source of gain or loss from the sale or exchange of personal property is generally determined by the residence of the seller, a foreign partner may have effectively connected income by reason of the asset use or business activities of the partnership in which he is an investor. Special rules apply to treat gain or loss from disposition of U.S. real property interests as effectively connected with the conduct of a U.S. trade or business. To the extent that consideration received by the nonresident alien or foreign corporation for all or part of its interest in a partnership is attributable to a U.S. real property interest, that consideration is considered to be received from the sale or exchange in the United States of such property. In certain circumstances, gain attributable to sales of U.S. real property interests may be subject to withholding tax of ten percent of the amount realized on the transfer.	[7] I.R.C. § 1446(f)(6). Congress intended that under this regulatory authority, the Secretary would provide "guidance permitting a broker, as agent of the transferee, to deduct and withhold the tax equal to 10 percent of the amount realized on the disposition of a partnership interest to which the provision applies. For example, such guidance may provide that if an interest in a publicly traded partnership is sold by a foreign partner through a broker, the broker may deduct and withhold the 10-percent tax on behalf of the transferee." [8] Tax Cuts and Jobs Act § 13501(a). [9] *Id.* § 13501(b).		§ 864(c) § 1446

J.1. - TREATMENT OF GAIN OR LOSS OF FOREIGN PERSONS FROM SALE OR EXCHANGE OF INTERESTS IN PARTNERSHIPS ENGAGED IN TRADE OR BUSINESS WITHIN THE US

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Under a 1991 revenue ruling, in determining the source of gain or loss from the sale or exchange of an interest in a foreign partnership, the IRS applied the asset-use test and business activities test at the partnership level to determine the extent to which income derived from the sale or exchange is effectively connected with that U.S. business. Under the ruling, if there is unrealized gain or loss in partnership assets that would be treated as effectively connected with the conduct of a U.S. trade or business if those assets were sold by the partnership, some or all of the foreign person's gain or loss from the sale or exchange of a partnership interest may be treated as effectively connected with the conduct of a U.S. trade or business. However, a 2017 Tax Court case rejects the logic of the ruling and instead holds that, generally, gain or loss on sale or exchange by a foreign person of an interest in a partnership that is engaged in a U.S. trade or business is foreign-source.			§ 864(c) § 1446

J.2. – MODIFICATION OF THE DEFINITION OF SUBSTANTIAL BUILT-IN LOSS IN THE CASE OF TRANSFER OF PARTNERSHIP INTEREST

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
In general, a partnership does not adjust the basis of partnership property following the transfer of a partnership interest unless either the partnership has made a one-time election under section 754 to make basis adjustments, or the partnership has a substantial built-in loss immediately after the transfer. If an election is in effect, or if the partnership has a substantial built-in loss immediately after the transfer, adjustments are made with respect to the transferee partner. These adjustments are to account for the difference between the transferee partner's proportionate share of the adjusted basis of the partnership property and the transferee's basis in its partnership interest. The adjustments are intended to adjust the basis of partnership property to approximate the result of a direct purchase of the property by the transferee partner. Under the provision, a substantial built-in loss exists if the partnership's adjusted basis in its property exceeds by more than $250,000 the fair market value of the partnership property. Certain securitization partnerships and electing investment partnerships are not treated as having a substantial built-in loss in certain instances, and thus are not required to make basis adjustments to partnership property. For electing investment partnerships, in lieu of the partnership basis adjustments, a partner-level loss limitation rule applies.	**1. In General.** The provision modifies the definition of a substantial built-in loss for purposes of section 743(d), affecting transfers of partnership interests. Under the provision, in addition to the present-law definition,[1] a substantial built-in loss also exists if the transferee would be allocated a net loss in excess of $250,000 upon a hypothetical sale by the partnership of all partnership's assets for cash equal to the assets' fair market value, immediately after the transfer of the partnership interest.[2] **2. Example.** For example, a partnership of three taxable partners (partners A, B, and C) has not made an election pursuant to section 754. The partnership has two assets, one of which, Asset X, has a built-in gain of $1 million, while the other asset, Asset Y, has a built-in loss of $900,000. Pursuant to the partnership agreement, any gain on sale or exchange of Asset X is specially allocated to partner A. The three partners share equally in all other partnership items, including in the built-in loss in Asset Y. In this case, each of partner B and partner C has a net built-in loss of $300,000 (one third of the loss attributable to asset Y) allocable to his partnership interest. Nevertheless, the partnership does not have an overall built-in loss, but a net built-in gain of $100,000 ($1 million minus $900,000). Partner C sells his partnership interest to another person, D, for $33,333. Under the provision, the test for a substantial built-in loss applies both at the partnership level and at the transferee partner level.	The provision applies to transfers of partnership interests after December 31, 2017.[3]	§ 743

J.2. – MODIFICATION OF THE DEFINITION OF SUBSTANTIAL BUILT-IN LOSS IN THE CASE OF TRANSFER OF PARTNERSHIP INTEREST

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	If the partnership were to sell all its assets for cash at their fair market value immediately after the transfer to D, D would be allocated a loss of $300,000 (one third of the built-in loss of $900,000 in Asset Y). A substantial built-in loss exists under the partner-level test added by the provision, and the partnership adjusts the basis of its assets accordingly with respect to D. [1] I.R.C. § 743(d)(1)(A). [2] I.R.C. § 743(d)(1)(B). [3] Tax Cuts and Jobs Act § 13502(b).		§ 743

J.3. - CHARITABLE CONTRIBUTIONS AND FOREIGN TAXES TAKEN INTO ACCOUNT IN DETERMINING LIMITATION ON ALLOWANCE OF PARTNER'S SHARE OF LOSS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
A partner's distributive share of partnership loss (including capital loss) is allowed only to the extent of the adjusted basis (before reduction by current year's losses) of the partner's interest in the partnership at the end of the partnership taxable year in which the loss occurred. Any disallowed loss is allowable as a deduction at the end of the first succeeding partnership taxable year, and subsequent taxable years, to the extent that the partner's adjusted basis for its partnership interest at the end of any such year exceeds zero (before reduction by the loss for the year). A partner's basis in its partnership interest is increased by its distributive share of income (including tax exempt income). A partner's basis in its partnership interest is decreased (but not below zero) by distributions by the partnership and its distributive share of partnership losses and expenditures of the partnership not deductible in computing partnership taxable income and not properly chargeable to capital account. In the case of a charitable contribution, a partner's basis is reduced by the partner's distributive share of the adjusted basis of the contributed property. A partnership computes its taxable income in the same manner as an individual with certain exceptions. The exceptions provide, in part, that the deductions for foreign taxes and charitable contributions are not allowed to the partnership. Instead, a partner takes into account its distributive share of the foreign taxes paid by the partnership and the charitable contributions made by the partnership for the taxable year.	**1. In General.** The provision modifies the basis limitation on partner losses to provide that the limitation takes into account a partner's distributive share of partnership charitable contributions (as defined in section 170(c)) and taxes (described in section 901) paid or accrued to foreign countries and to possessions of the United States.[1] Thus, the amount of the basis limitation on partner losses is decreased to reflect these items. **2. Example.** In the case of a charitable contribution by the partnership, the amount of the basis limitation on partner losses is decreased by the partner's distributive share of the adjusted basis of the contributed property.[2] **3. Exception.** In the case of a charitable contribution by the partnership of property whose fair market value exceeds its adjusted basis, a special rule provides that the basis limitation on partner losses does not apply to the extent of the partner's distributive share of the excess.[3] [1] I.R.C. § 704(d)(3)(A). [2] *See* I.R.C. §§ 702(a)(4); see also 170(e)(1) (stating generally that the gain on any charitable contribution of property is not included as a deduction, except for long-term capital gain in certain contributions). [3] I.R.C. § 704(d)(3)(B). [4] Tax Cuts and Jobs Act § 13503(b).	The provision applies to partnership taxable years beginning after December 31, 2017.[4]	§ 704

J.3. - CHARITABLE CONTRIBUTIONS AND FOREIGN TAXES TAKEN INTO ACCOUNT IN DETERMINING LIMITATION ON ALLOWANCE OF PARTNER'S SHARE OF LOSS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
However, in applying the basis limitation on partner losses, Treasury regulations do not take into account the partner's share of partnership charitable contributions and foreign taxes paid or accrued. The IRS has taken the position in a private letter ruling that the basis limitation on partner losses does not apply to limit the partner's deduction for its share of the partnership's charitable contributions. While the regulations relating to the loss limitation do not mention the foreign tax credit, a taxpayer may choose the foreign tax credit in lieu of deducting foreign taxes. By contrast, under S corporation rules limiting the losses and deductions which may be taken into account by a shareholder of an S corporation to the shareholder's basis in stock and debt of the corporation, the shareholder's pro rata share of charitable contributions and foreign taxes are taken into account. In the case of charitable contributions, a special rule is provided prorating the amount of appreciation not subject to the limitation in the case of charitable contributions of appreciated property by the S corporation.			§ 704

J.5. – EXPANSION OF QUALIFYING BENEFICIARIES OF AN ELECTING SMALL BUSINESS TRUST

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
An electing small business trust ("ESBT") may be a shareholder of an S corporation. Generally, the eligible beneficiaries of an ESBT include individuals, estates, and certain charitable organizations eligible to hold S corporation stock directly. A nonresident alien individual may not be a shareholder of an S corporation and may not be a potential current beneficiary of an ESBT. The portion of an ESBT which consists of the stock of an S corporation is treated as a separate trust and generally is taxed on its share of the S corporation's income at the highest rate of tax imposed on individual taxpayers. This income (whether or not distributed by the ESBT) is not taxed to the beneficiaries of the ESBT.	The provision allows a nonresident alien individual to be a potential current beneficiary of an Electing Small Business Trust.[1] [1] *See* I.R.C. § 1351(c)(2)(B)(v). [2] Tax Cuts and Jobs Act § 13541(b).	The provision takes effect on January 1, 2018.[2]	§ 1361

J.6. - CHARITABLE CONTRIBUTION DEDUCTION FOR ELECTING SMALL BUSINESS TRUSTS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
An electing small business trust ("ESBT") may be a shareholder of an S corporation. The portion of an ESBT that consists of the stock of an S corporation is treated as a separate trust and generally is taxed on its share of the S corporation's income at the highest rate of tax imposed on individual taxpayers. This income (whether or not distributed by the ESBT) is not taxed to the beneficiaries of the ESBT. In addition to nonseparately computed income or loss, an S corporation reports to its shareholders their pro rata share of certain separately stated items of income, loss, deduction, and credit. For this purpose, charitable contributions (as defined in section 170(c)) of an S corporation are separately stated and taken by the shareholder. The treatment of a charitable contribution passed through by an S corporation depends on the shareholder. Because an ESBT is a trust, the deduction for charitable contributions applicable to trusts, rather than the deduction applicable to individuals, applies to the trust. Generally, a trust is allowed a charitable contribution deduction for amounts of gross income, without limitation, which pursuant to the terms of the governing instrument are paid for a charitable purpose. No carryover of excess contributions is allowed. An individual is allowed a charitable contribution deduction limited to certain percentages of adjusted gross income generally with a five-year carryforward of amounts in excess of this limitation.	Under the provision, the charitable contribution deduction of an Electing Small Business Trust (ESBT) is not determined by the rules generally applicable to trusts but rather by the rules applicable to individuals.[1] Thus, the percentage limitations and carryforward provisions applicable to individuals apply to charitable contributions made by the portion of an ESBT holding S corporation stock.[2] [1] I.R.C. § 641(c)(2)(E). [2] *See* I.R.C. § 641(c)(1), (2); § 170. [3] Tax Cuts and Jobs Act § 13542(b).	The provision applies to taxable years beginning after December 31, 2017.[3]	§ 642(C)

J.16. - AMOUNTS PAID FOR AIRCRAFT MANAGEMENT SERVICES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Excise tax on taxable transportation by air For domestic passenger transportation, section 4261 imposes an excise tax on amounts paid for taxable transportation. In general, for domestic flights, the tax consists of two parts: a 7.5 percent ad valorem tax applied to the amount paid and a flat dollar amount for each flight segment (consisting of one takeoff and one landing). "Taxable transportation" generally means transportation by air which begins and ends in the United States. The tax is paid by the person making the payment subject to tax and the tax is collected by the person receiving the payment. For commercial freight aviation, the ad valorem tax is 6.25 percent of the amount paid for transportation. In determining whether a flight constitutes taxable transportation and whether the amounts paid for such transportation are subject to tax, the Internal Revenue Service ("IRS") has looked at who has "possession, command, and control" of the aircraft based on the relevant facts and circumstances. **Applicability to aircraft management services** Generally, an aircraft management services company ("management company") has as its business purpose the management of aircraft owned by other corporations or individuals ("aircraft owners"). In this function, management companies provide aircraft owners, among other things, with administrative and support services (such as scheduling, flight planning, and weather forecasting), aircraft maintenance services, the provision of pilots and crew, and compliance with regulatory standards.	1. **Exemption from Excise Taxes.** The provision exempts certain payments related to the management of private aircraft from the excise taxes imposed on taxable transportation by air.[1] **2. Qualifying Exempt Payments.** Exempt payments are those amounts paid by an aircraft owner for certain management services related to maintenance and support of the owner's aircraft or flights on the aircraft owner's aircraft..[2] 3. **Management Services.** Applicable services include: a. Support activities related to the aircraft itself, such as its storage, maintenance, and fueling;[3] b. Support activities related to the aircraft's operation, such as the hiring and training of pilots and crew, as well as administrative services such as scheduling, flight planning, weather forecasting, obtaining insurance, and establishing and complying with safety standards;[4] and c. Other services as are necessary to support flights operated by an aircraft owner.[5] [1] I.R.C. § 4261(e)(5)(A); *see* I.R.C. §§ 4261(a), 4271(a). [2] I.R.C. § 4261(e)(5)(A). [3] I.R.C. § 4261(e)(5)(B)(iii). [4] I.R.C. § 4261(e)(5)(B)(i), (ii), (iv), (v). [5] I.R.C. § 4261(e)(5)(B)(vi). [6] Tax Cuts and Jobs Act § 13822(b).	The provision is effective for amounts paid after the date of enactment.[6]	§ 4261

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Although the arrangement between management companies and aircraft owners may vary, it is our understanding that aircraft owners generally pay management companies a monthly fee to cover the fixed expenses of maintaining the aircraft (such as insurance, maintenance, and recordkeeping) and a variable fee to cover the cost of using the aircraft (such as the provision of pilots, crew, and fuel). In March 2012, the IRS issued a Chief Counsel Advice determining that a management company provided all of the essential elements necessary for providing transportation by air and the owner relinquished possession, command and control to the management company. Thus, the management company was determined to be providing taxable transportation to the owner and was required to collect the appropriate federal excise tax from the aircraft owner and remit it to the IRS. The Chief Counsel Advice resulted in increased audit activity by the IRS on aircraft management companies. In May 2013, the IRS suspended assessment of the federal excise tax with respect to aircraft management services while it developed guidance on the tax treatment of aircraft management issues. In a 2015 opinion, an Ohio district court held that the existing revenue rulings (in effect for the tax period April 1, 2005, through June 30, 2009, the period that was the subject of the litigation) regarding the possession, command and control test, failed to provide precise and not speculative notice of a collection obligation as it related to whole-aircraft management contracts.			§ 4261

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As a result, the court ruled as a matter of law that because precise and not speculative notice was not received, the aircraft management company plaintiff did not have a collection obligation with respect to the Federal excise tax on payments received for whole- aircraft management services. In 2017, the IRS decided not to pursue examination of the issue of whether amounts paid to aircraft companies by the owners or lessors of the aircraft are taxable until further guidance is made available. According to the IRS, for any exam in suspense the aircraft management fee issue was conceded and the taxpayers were notified accordingly. The IRS has not issued further guidance on this issue.			§ 4261

Tax Reform
Section A

A.1. - INCREASE IN STANDARD DEDUCTION

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Under present law, an individual who does not elect to itemize deductions may reduce his or her adjusted gross income ("AGI") by the amount of the applicable standard deduction in arriving at his or her taxable income. The standard deduction is the sum of the basic standard deduction and, if applicable, the additional standard deduction. The basic standard deduction varies depending upon a taxpayer's filing status. For 2017, the amount of the basic standard deduction is $6,350 for single individuals and married individuals filing separate returns, $9,350 for heads of households, and $12,700 for married individuals filing a joint return and surviving spouses. An additional standard deduction is allowed with respect to any individual who is elderly or blind. The amount of the standard deduction is indexed annually for inflation. In the case of a dependent for whom a deduction for a personal exemption is allowed to another taxpayer, the standard deduction may not exceed the greater of (i) $1,050 (in 2017) or (ii) the sum of $350 (in 2017) plus the individual's earned income.	**1. Temporary Increase in Standard Deduction.** The Act temporarily increases the basic standard deduction for individuals across all filing statuses. Under the provision, the amount of the standard deduction is temporarily increased to $24,000 for married individuals filing a joint return, $18,000 for head- of-household filers, and $12,000 for all other individuals.[1] The amount of the standard deduction is indexed for inflation using the C-CPI-U for taxable years beginning after December 31, 2018.[2] The additional standard deduction for the elderly and the blind is not changed by the provision. **2. Expiration of Temporary Increase.** The increase of the basic standard deduction does not apply to taxable years beginning after December 31, 2025.[3] [1] I.R.C. § 63(c)(7)(A). [2] I.R.C. § 63(c)(7)(B). [3] I.R.C. § 63(c)(7). [4] Act Sec. 11011(e).	The provision is effective for taxable years beginning after December 31, 2017.[4]	§ 63

A.2. – REPEAL OF THE DEDUCTION FOR PERSONAL EXEMPTIONS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Under present law, in determining taxable income, an individual reduces AGI by any personal exemption deductions and either the applicable standard deduction or his or her itemized deductions. Personal exemptions generally are allowed for the taxpayer, his or her spouse, and any dependents. For 2017, the amount deductible for each personal exemption is $4,050. This amount is indexed annually for inflation. The personal exemption amount is phased out in the case of an individual with AGI in excess of $313,800 for married taxpayers filing jointly, $287,650 for heads of household, $156,900 for married taxpayers filing separately, and $261,500 for all other filers. In addition, no personal exemption is allowed in the case of a dependent if a deduction is allowed to another taxpayer. **Withholding rules** Under present law, the amount of tax required to be withheld by employers from a taxpayer's wages is based in part on the number of withholding exemptions a taxpayer claims on his Form W-4. An employee is entitled to the following exemptions: (1) an exemption for himself, unless he allowed to be claimed as a dependent of another person; (2) an exemption to which the employee's spouse would be entitled, if that spouse does not file a Form W-4 for that taxable year claiming an exemption described in (1); (3) an exemption for each individual who is a dependent (but only if the employee's spouse has not also claimed such a withholding exemption on a Form W-4); (4) additional withholding allowances (taking into account estimated itemized deductions, estimated tax credits, and additional deductions as provided by the Secretary of the Treasury); and (5) a standard deduction allowance.	**Suspension of Deduction for Personal Exemptions.** The Act suspends the deduction for personal exemptions.[1] The provision does not apply to taxable years beginning after December 31, 2025.[2] [1] I.R.C. § 151(d)(5). [2] I.R.C. § 151(d)(5). [3] Act Sec. 11041(f).	The provision is effective for taxable years beginning after December 31, 2017.[3]	§ 151

A.2. – REPEAL OF THE DEDUCTION FOR PERSONAL EXEMPTIONS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Filing requirements Under present law, an unmarried individual is required to file a tax return for the taxable year if in that year the individual had income which equals or exceeds the exemption amount plus the standard deduction applicable to such individual (*i.e.*, single, head of household, or surviving spouse). An individual entitled to file a joint return is required to do so unless that individual's gross income, when combined with the individual's spouse's gross income for the taxable year, is less than the sum of twice the exemption amount plus the basic standard deduction applicable to a joint return, provided that such individual and his spouse, at the close of the taxable year, had the same household as their home. **Trusts and estates** In lieu of the deduction for personal exemptions, an estate is allowed a deduction of $600. A trust is allowed a deduction of $100; $300 if required to distribute all its income currently; and an amount equal to the personal exemption of an individual in the case of a qualified disability trust.			§ 151

Tax Reform
Section B

B.1. – DEDUCTION FOR QUALIFIED BUSINESS INCOME

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Individual income tax rates To determine regular tax liability, an individual taxpayer generally must apply the tax rate schedules (or the tax tables) to his or her regular taxable income. The rate schedules are broken into several ranges of income, known as income brackets, and the marginal tax rate increases as a taxpayer's income increases. Separate rate schedules apply based on an individual's filing status (i.e., single, head of household, married filing jointly, or married filing separately). For 2017, the regular individual income tax rate schedule provides rates of 10, 15, 25, 28, 33, 35, and 39.6 percent. **Partnerships** Partnerships generally are treated for Federal income tax purposes as pass-through entities not subject to tax at the entity level. Items of income (including tax-exempt income), gain, loss, deduction, and credit of the partnership are taken into account by the partners in computing their income tax liability (based on the partnership's method of accounting and regardless of whether the income is distributed to the partners). A partner's deduction for partnership losses is limited to the partner's adjusted basis in its partnership interest. Losses not allowed as a result of that limitation generally are carried forward to the next year. A partner's adjusted basis in the partnership interest generally equals the sum of (1) the partner's capital contributions to the partnership, (2) the partner's distributive share of partnership income, and (3) the partner's share of partnership liabilities, less (1) the partner's distributive share of losses allowed as a deduction and certain nondeductible expenditures, and (2) any partnership distributions to the partner. Partners generally may receive distributions of partnership property without recognition of gain or loss, subject to some exceptions.	**A. Deduction Allowed.** **1. Amount of Deduction Allowed and Overall Limitation.** **a. Amount of Deduction.** A noncorporate taxpayer is allowed a deduction (the "QBI Deduction") or the tax year equal to the sum of: (1) The lesser of (1) the combined qualified business income amount of the taxpayer;[1] or (2) an amount equal to 20 percent of the excess of the taxpayer's taxable income over any net capital gain and qualified cooperative dividends;[2] plus (2) The lesser of (1) 20 percent of qualified cooperative dividends; (2) taxable income (reduced by net capital gain).[3] **b. Overall Limitation on Deduction.** The QBI Deduction is limited to the taxpayer's taxable income for the taxable year (reduced by net capital gain).[4] **c. Computation of Taxable Income.** For purposes of Section 199A, taxable income is determined without regard to the deduction allowable under Section 199A.[5] **d. Deduction Allowed Only for Federal Income Tax Purposes.** The deduction under the provision is allowed only for Federal income tax purposes.[6] **e. Termination.** Section 199A does not apply to taxable years beginning after December 31, 2025.[7] **2. Determine Combined Qualified Business Income Amount.** The combined qualified business income amount for the taxable year is the sum of (a) the deductible amounts	The provision is effective for taxable years beginning after December 31, 2017.[82]	§ 199A

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Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Partnerships may allocate items of income, gain, loss, deduction, and credit among the partners, provided the allocations have substantial economic effect. In general, an allocation has substantial economic effect to the extent the partner to which the allocation is made receives the economic benefit or bears the economic burden of such allocation and the allocation substantially affects the dollar amounts to be received by the partners from the partnership independent of tax consequences. State laws of every State provide for limited liability companies ("LLCs"), which are neither partnerships nor corporations under applicable State law, but which are generally treated as partnerships for Federal tax purposes. Under present law, a publicly traded partnership generally is treated as a corporation for Federal tax purposes. For this purpose, a publicly traded partnership means any partnership if interests in the partnership are traded on an established securities market or interests in the partnership are readily tradable on a secondary market (or the substantial equivalent thereof). An exception from corporate treatment is provided for certain publicly traded partnerships, 90 percent or more of whose gross income is qualifying income. **<u>S corporations</u>** For Federal income tax purposes, an S corporation generally is not subject to tax at the corporate level. Items of income (including tax-exempt income), gain, loss, deduction, and credit of the S corporation are taken into account by the S corporation shareholders in computing their income tax liabilities (based on the S corporation's method of	determined for each qualified trade or business carried on by the taxpayer and (b) 20 percent of the taxpayer's qualified REIT dividends and qualified publicly traded partnership income. **a. Step 1: Identify all of the Taxpayer's Trade or Businesses.** The first step in the analysis is to identify all of the taxpayer's trades or businesses. **b. Step 2: Identify all of the Taxpayer's Qualified Trades or Businesses.** A qualified trade or business means any trade or business other than (1) a specified service trade or business;[10] and (2) other than the trade or business of performing services as an employee.[11] **(1) Step 2(a): Determine whether the taxpayer's trade or business is the trade or business of performing services as an employee.** If the taxpayer's trade or business is the trade or business of performing services as an employee, such trade or business is not a qualified trade or business. **(2) Step 2(b): Determine whether the taxpayer's trade or business is a specified trade or business.** If the taxpayer's trade or business is a specified trade or business, unless a limited exception applies based upon the taxpayer's income, such trade or business is not a qualified trade or business. **i) Step 2(b)(1): Apply the Definition of Specified Service Trade or Business to the Taxpayer's Activity and Determine If the Taxpayer's Trade or Business is a Specified Service Trade or Business.** A specified service trade or business means any		§ 199A

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Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
accounting and regardless of whether the income is distributed to the shareholders). A shareholder's deduction for corporate losses is limited to the sum of the shareholder's adjusted basis in its S corporation stock and the indebtedness of the S corporation to such shareholder. Losses not allowed as a result of that limitation generally are carried forward to the next year. A shareholder's adjusted basis in the S corporation stock generally equals the sum of (1) the shareholder's capital contributions to the S corporation and (2) the shareholder's pro rata share of S corporation income, less (1) the shareholder's pro rata share of losses allowed as a deduction and certain nondeductible expenditures, and (2) any S corporation distributions to the shareholder. In general, an S corporation shareholder is not subject to tax on corporate distributions unless the distributions exceed the shareholder's basis in the stock of the corporation. **<u>Electing S corporation status</u>** To be eligible to elect S corporation status, a corporation may not have more than 100 shareholders and may not have more than one class of stock. Only individuals (other than nonresident aliens), certain tax-exempt organizations, and certain trusts and estates are permitted shareholders of an S corporation. **<u>Sole proprietorships</u>** Unlike a C corporation, partnership, or S corporation, a business conducted as a sole proprietorship is not treated as an entity distinct from its owner for Federal income tax purposes. Rather, the business owner is taxed directly on business income, and files Schedule C (sole proprietorships generally), Schedule E (rental real estate and	trade or business involving the performance of services in the fields of health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services, or any trade or business where the principal asset of such trade or business is the reputation or skill of one or more of its employees or owners, or which involves the performance of services that consist of investing and investment management trading, or dealing in securities, partnership interests, or commodities. For this purpose a security and a commodity have the meanings provided in the rules for the mark-to-market accounting method for dealers in securities (sections 475(c)(2) and 475(e)(2), respectively).[12] **ii) Step 2(b)(2): If the Taxpayer's Trade or Business is a Specified Service Trade or Business, Determine Whether Limited Relief is Available Based Upon the Taxpayer's Income.** The exclusion from the definition of a qualified business for specified service trades or businesses phases in for a taxpayer with taxable income in excess of a threshold amount.[13] The exclusion from the definition of a qualified business for specified service trades or businesses is fully phased in for a taxpayer with taxable income in excess of the threshold amount plus $50,000 ($100,000 in the case of a joint return).[14] **c. Step 3: Determine the Deductible Amount for Each Qualified Trade or Business Carried On By The Taxpayer.[15]** The third step is to determine the deductible amount for each qualified trade or business carried on by the taxpayer. For each qualified trade or business, the taxpayer is allowed a deductible amount equal		§ 199A

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Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
royalties), or Schedule F (farms) with his or her individual tax return. Furthermore, transfer of a sole proprietorship is treated as a transfer of each individual asset of the business. Nonetheless, a sole proprietorship is treated as an entity separate from its owner for employment tax purposes, for certain excise taxes, and certain information reporting requirements.	to the lesser of: (1) 20 percent of the qualified business income with respect to such trade or business;[16] or (2) the greater of (the "***Wage Limit***"): (a) 50 percent of the W-2 wages paid with respect to the qualified trade or business (the "***Wages Paid Limit***"), or (b) the sum of 25 of percent of the W-2 wages with respect to the qualified trade or business plus 2.5 percent of the unadjusted basis, immediately after acquisition, of all qualified property (the "***Wages Paid Plus a Capital Element Limit***").[17] **(1) Step 3(a): Determine Qualified Business Income of Each Qualified Trade or Business.** For any taxable year, qualified business income means the net amount of qualified items of income, gain, deduction, and loss with respect to the qualified trade or business of the taxpayer.[18] The term does not include aggregate qualified REIT dividends, qualified cooperative dividends, and qualified publicly traded partnership income.[19] Qualified business income is determined without regard to any adjustments prescribed by Section 56 through 59 of the alternative minimum tax.[20] **(a) Qualified Items Taken Into Account Only To the Extent Included or Allowed in Determining Taxable Income**. The determination of qualified items of income, gain, deduction, and loss takes into account these items only to the extent included or allowed in the determination of taxable income for the year.[21] For example, if in a taxable year, a qualified business has $100,000 of ordinary income from inventory sales, and makes an expenditure of $25,000 that is required to be capitalized and amortized over 5 years under applicable tax		§ 199A

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	rules, the qualified business income is $100,000 minus $5,000 (current-year ordinary amortization deduction), or $95,000. The qualified business income is not reduced by the entire amount of the capital expenditure, only by the amount deductible in determining taxable income for the year.[22] **(b) Qualified Items Do Not Include Investment-Related Income. Qualified items do not include specified investment-related income, deductions, or loss.[23]** Specifically, qualified items of income, gain, deduction and loss do not include (1) any item of short-term capital gain, short-term capital loss, long-term capital gain, or long-term capital loss.;[24] (2) dividends, income equivalent to a dividend, or payments in lieu of dividends;[25] (3) interest income other than that which is properly allocable to a trade or business;[26] (4) the excess of gain over loss from commodities transactions;[27] (5) the excess of foreign currency gains over foreign currency losses from section 988 transactions, other than transactions directly related to the business needs of the business activity;[28] (6) net income from notional principal contracts, other than clearly identified hedging transactions that are treated as ordinary (i.e., not treated as capital assets);[29] and (7) any amount received from an annuity that is not used in the trade or business of the business activity.[30] Qualified items under this provision do not include any item of deduction or loss properly allocable to such income.[31] **(c) Domestic Business.** Items are treated as qualified items of income, gain, deduction, and loss only to the extent they are effectively connected with the conduct of a		§ 199A

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	trade or business within the United States.[32] In the case of a taxpayer who is an individual with otherwise qualified business income from sources within the commonwealth of Puerto Rico, if all the income is taxable under income tax rates for individuals for the taxable year, the "United States" is considered to include Puerto Rico for purposes of determining the individual's qualified business income.[33] **(d) Reasonable compensation and guaranteed payments.** Qualified business income does not include: i) Reasonable compensation paid to the taxpayer by any qualified trade or business of the taxpayer for services rendered with respect to the trade or business;[34] ii) Any guaranteed payment (described in Section 707(c) for services rendered with respect to the trade or business;[35] and iii) To the extent provided in regulations, does not include any amount paid or incurred by a partnership to a partner who is acting other than in his or her capacity as a partner for services.[36] **(2) Step 3(b): Calculate Wage Limit.** The Wage Limit is the greater of: (a) 50 percent of the W-2 wages paid with respect to the qualified trade or business (the "Wages Paid Limit"); or (b) the sum of 25 percent of the W-2 wages with respect to the qualified trade or business plus 2.5 percent of the unadjusted basis, immediately after acquisition, of all qualified property (the "Wages Paid Plus a Capital Element Limit"). If the taxpayer's taxable income is below a threshold amount, the deductible amount for each qualified trade or business is determined without regard to the Wage Limit and is equal to 20 percent of the		§ 199A

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	qualified business income with respect to each respective trade or business.[37] **(a) Step 3(b)(1): Determine Whether Taxable Income Is Below the Threshold Amount.** If the taxpayer's taxable income is below the threshold amount, the deductible amount for each qualified trade or business is determined without regard to the Wage Limit and the deductible amount is equal to 20 percent of the qualified business income with respect to each respective trade or business.[38] The threshold amount is \$157,500 (twice that amount or \$315,000 in the case of a joint return),[39] indexed for inflation in the case of tax years beginning after 2018.[40] The conferees expect that the reduced threshold amount will serve to deter high-income taxpayers from attempting to convert wages or other compensation for personal services to income eligible for the 20-percent deduction under the provision. **(b) Step 3(b)(2): Determine W-2 Wages.** **i) Amounts Included in Total Wages.** W-2 wages are the total wages subject to wage withholding,[41] elective deferrals,[42] and deferred compensation[43] paid by the qualified trade or business with respect to employment of its employees during the calendar year ending during the taxable year of the taxpayer.[44] **ii) Limitation to Wages Attributable to Qualified Business Income.** W-2 wages do not include any amount which is not properly allocable to the qualified business income as a qualified item of deduction.[45]		§ 199A

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	iii) Return Requirement. W-2 wages do not include any amount which was not properly included in a return filed with the Social Security Administration on or before the 60th day after the due date (including extensions) for such return.[46] **(c) Step 3(b)(3): Identify Qualified Property.** Qualified property means tangible property of a character subject to depreciation that is held by, and available for use in, the qualified trade or business at the close of the taxable year,[47] and which is used in the production of qualified business income,[48] and for which the depreciable period has not ended before the close of the taxable year.[49] The depreciable period with respect to qualified property of a taxpayer means the period beginning on the date the property is first placed in service by the taxpayer and ending on the later of (a) the date 10 years after that date,[50] or (b) the last day of the last full year in the applicable recovery period that would apply to the property under section 168 (without regard to section 168(g)).[51] In the case of property that is sold, for example, the property is no longer available for use in the trade or business and is not taken into account in determining the limitation.[52] Treasury is required to provide rules for applying the limitation in cases of a short taxable year of where the taxpayer acquires, or disposes of, the major portion of a trade or business or the major portion of a separate unit of a trade or business during the year.[53] Treasury is expected to provide guidance applying rules similar to the rules of section 179(d)(2) to address acquisitions of property from a related party,[54] as well as in a sale-leaseback		§ 199A

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	or other transaction as needed to carry out the purposes of the provision and to provide anti-abuse rules, including under the limitation based on W-2 wages and capital. Similarly, Treasury is expected to provide guidance prescribing rules for determining the unadjusted basis immediately after acquisition of qualified property acquired in like-kind exchanges or involuntary conversions[55] as needed to carry out the purposes of the provision and to provide anti-abuse rules, including under the limitation based on W-2 wages and capital.[56] **(d) Step 3(b)(4): Apply Phase-in Wage Limitation Rules, If Applicable.** The application of the wage limit phases in for a taxpayer with taxable income in excess of the threshold amount.[57] The wage limit applies fully for a taxpayer with taxable income in excess of the threshold amount plus $50,000 ($100,000 in the case of a joint return).[58] For a taxpayer with taxable income within the phase-in range, the wage limit applies as follows: **i) Step 3(b)(4)(i):** With respect to any qualified trade or business, the taxpayer compares (1) 20 percent of the taxpayer's qualified business income with respect to the qualified trade or business, with (2) the Wage Limit.[59] **ii) Step 3(b)(4)(ii):** If the Wage Limit is less than 20% of the taxpayer's qualified business income (that is, if the wage limit is binding),[60] the taxpayer's deductible amount is the amount determined as 20% of qualified business income reduced[61] by the same proportion of the difference between the two		§ 199A

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	amounts[62] as the excess of the taxable income of the taxpayer over the threshold amount bears to $50,000 ($100,000 in the case of a joint return).[63] **d. Step 4: Determine Qualified REIT Dividends, Cooperative Dividends, and Publicly Traded Partnership Income**. **(1) Qualified REIT Dividends.** Qualified REIT dividends means any dividend from a REIT received during the tax year, but does not include any portion of a dividend received from a REIT that is a capital gain dividend (as defined in Section 857(b)(3)) or a qualified dividend (as defined in Section 1(h)(11)).[65] **(2) Qualified Cooperative Dividends**. Qualified cooperative dividend means a patronage dividend (as defined in Section 1388(a)), any per-unit retain allocation (I.R.C. 1388(f)), any qualified written notice of allocation (I.R.C. 1388(c)) or any similar amount, provided it is includible in gross income and is received from either (1) a tax-exempt benevolent life insurance association, mutual ditch or irrigation company, cooperative telephone company or like cooperative organization, or a taxable or tax-exempt cooperative that is described in section 1381(a),[66] or (2) a taxable cooperative governed by tax rules applicable to cooperatives before the enactment of subchapter T of the Code in 1962.[67]		§ 199A

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	(3) Qualified Publicly Traded Partnership Income. Qualified publicly traded partnership income means (with respect to any qualified trade or business of the taxpayer), the sum of the (a) the net amount of the taxpayer's allocable share of each qualified item of income, gain, deduction, and loss (that are effectively connected with a U.S. trade or business and are included or allowed in determining taxable income for the taxable year and do not constitute excepted enumerated investment-type income, and not including the taxpayer's reasonable compensation, guaranteed payments for services, or (to the extent provided in regulations) section 707(a) payments for services) from a publicly traded partnership not treated as a corporation,[68] and (b) gain recognized by the taxpayer on disposition of its interest in the partnership that is treated as ordinary income under Section 751(a).[69] **e. Step 5: Consider Special Rules for Partnerships, S Corporations, Trusts and Estates.** **(1) Application to Partnerships and S Corporations.** In the case of a partnership or S corporation, Section 199A applies at the partner or shareholder level.[70] Each partner takes into account the partner's allocable share of each qualified item of income, gain, deduction, and loss,[71] and is treated as having W-2 wages and unadjusted tax basis immediately after		§ 199A

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	acquisition of qualified property for the taxable year equal to the partner's allocable share of W-2 wages of the partnership and the unadjusted basis immediately after acquisition of qualified property of the partnership or S corporation for the taxable year (as determined under regulations to be issued by Treasury).[72] The partner's allocable share of W-2 wages is required to be determined in the same manner as the partner's share of wage expenses.[73] **(2) Application to Trusts and estates.** Trusts and estates are eligible for the 20-percent deduction under the provision. Conf. Report. Rules similar to the rules under present-law section 199 (as in effect on December 1, 2017) apply for apportioning between fiduciaries and beneficiaries any W-2 wages and unadjusted basis of qualified property under the limitation based on W-2 wages and capital.[74] **(3) Special Rules Apply to Specified Agricultural or Horticultural Cooperatives.** Special rules are provided for determining the deduction allowed to specified agricultural or horticultural cooperatives.[75] **B. Carryover of Losses.** If the net amount of qualified business income from all qualified trades or businesses during the taxable year is a loss, it is carried forward as a loss from a qualified trade or business in the next taxable year.[76] Similar to a qualified trade or business that has a qualified business loss for the current taxable year, any deduction allowed in a subsequent year is reduced (but not below zero) by 20 percent of any carryover qualified business loss.[77]		§ 199A

B.1. – DEDUCTION FOR QUALIFIED BUSINESS INCOME

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	C. Regulatory Authority. Authority is provided to promulgate regulations needed to carry out the purposes of the provision,[78] including regulations requiring, or restricting, the allocation of items of income, gain, loss, or deduction, or of wages under the provision.[79] In addition, regulatory authority is provided to address reporting requirements appropriate under the provision,[80] and the application of the provision in the case of tiered entities.[81]		§ 199A

[1] I.R.C. § 199A(a)(1)(A).

[2] I.R.C. § 199A(a)(1)(B).

[3] I.R.C. § 199A(a)(2).

[4] I.R.C. § 199A(a).

[5] I.R.C. § 199A(e)(1).

[6] I.R.C. § 199A(f)(3).

[7] I.R.C. § 199A(i).

[8] I.R.C. § 199A(b)(1)(A).

[9] I.R.C. § 199(b)(1)(B).

[10] I.R.C. § 199A(d)(1)(A)

[11] I.R.C. § 199A(d)(1)(B).

[12] I.R.C. § 199A(d)(2).

[13] I.R.C. § 199A(d)(3).

[14] I.R.C. § 199A(d)(3).

[15] I.R.C. § 199A(b)(1)(A); Conf. Rpt.

[16] I.R.C. § 199A(b)(2)(A).

[17] I.R.C. § 199A(b)(2)(B)(ii).

[18] I.R.C. § 199A(c).

[19] I.R.C. § 199A(c).

B.1. – DEDUCTION FOR QUALIFIED BUSINESS INCOME

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	[20] I.R.C. § 199A(f)(2). [21] I.R.C. § 199A(c)(3)(A)(i); Conf. Rept. [22] Conf. Rept. [23] I.R.C. § 199A(c)(3)(B). [24] I.R.C. § 199A(c)(3)(B)(i). [25] I.R.C. § 199A(c)(3)(B)(ii). [26] I.R.C. § 199A(c)(3)(B)(iii) [27] I.R.C. § 199A(c)(3)(B)(iv) [28] I.R.C. § 199A(c)(3)(B)(iv); I.R.C. § 954(c)(1)(D). [29] I.R.C. § 199A(c)(3)(B)(v). [30] I.R.C. § 199(c)(3)(B)(vi). [31] I.R.C. § 199(c)(3)(B)(vii). [32] I.R.C. § 199A(c)(3)(A)(ii). For this purpose, section 864(c) is applied substituting "qualified trade or business (within the meaning of section 199A)" for "nonresident alien individual or a foreign corporation" or "a foreign corporation." [33] I.R.C. § 199A(f)(1)(C)(i). [34] I.R.C. § 199A(c)(4)(A). [35] I.R.C. § 199A(c)(4)(B). [36] I.R.C. § 199A(c)(4)(C). [37] I.R.C. § 199A(b)(3)(A). [38] I.R.C. § 199A(b)(3)(A). [39] I.R.C. § 199A(e)(2)(A). [40] I.R.C. § 199A(e)(2)(B). [41] Total wages is defined by reference to Section 3401(a). I.R.C. § 199A(b)(4)(A); *see* I.R.C. § 6051(a)(3). [42] I.R.C. § 6051(a)(8). [43] I.R.C. § 6051(a)(8).		§ 199A

B.1. – DEDUCTION FOR QUALIFIED BUSINESS INCOME

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	[44] I.R.C. § 199A(b)(4)(A); Conf. Rpt. [45] I.R.C. § 199A(b)(4)(B). [46] I.R.C. § 199A(b)(4)(C). [47] I.R.C. § 199A(b)(6)(A)(i). [48] I.R.C. § 199A(b)(6)(A)(ii). [49] I.R.C. § 199A(b)(6)(A)(iii). [50] I.R.C. § 199A(b)(6)(B)(i). [51] I.R.C. § 199A(b)(6)(B)(ii). [52] Conf. Report. [53] I.R.C. § 199A(b)(5). [54] I.R.C. § 199A(h)(1). [55] I.R.C. § 199A(h)(2). [56] Conf. report. [57] *See* I.R.C. § 199A(b)(3). [58] I.R.C. § 199A(b)(3). [59] I.R.C. § 199A(b)(3)(B). [60] I.R.C. § 199A(b)(3)(B)(i)(II). [61] I.R.C. § 199A(b)(3)(B)(I) [62] I.R.C. § 199A(b)(3)(B)(ii). [63] I.R.C. § 199A(b)(3)(B)(ii). [64] $520,000-$500,000)/$100,000 = 20 percent. [65] I.R.C. § 199A(e)(3). [66] I.R.C. § 199A(e)(4)(B)(i). [67] I.R.C. § 199A(e)(4)(B)(ii). [68] I.R.C. § 199A(e)(5)(A). [69] I.R.C. § 199A(e)(5)(B). [70] I.R.C. § 199A(f)(1)(A)(i). [71] I.R.C. § 199A(f)(1)(A)(ii).		§ 199A

B.1. – DEDUCTION FOR QUALIFIED BUSINESS INCOME

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	[72] I.R.C. § 199A(f)(1)(A)(iii). [73] I.R.C. § 199A(f)(1)(A)(iii). [74] I.R.C. § 199A(f)(1)(B). [75] *See* I.R.C. § 199A(g). [76] I.R.C. § 199A(c)(2). [77] Senate Report. [78] I.R.C. § 199A(f)(4). [79] I.R.C. § 199A(f)(4)(A). [80] I.R.C. § 199A(f)(4)(A). [81] I.R.C. § 199A(f)(4)(B). [82] Sec. 11011(e), P.L. 115-97, 12/22/2017.		§ 199A

B.1. – DEDUCTION FOR QUALIFIED BUSINESS INCOME

EXAMPLES	ANSWERS
1. Assume Taxpayer has qualified business income and taxable income of $100,000 related to a business that is not a specified service trade or business. The business incurred W-2 wages of $50,000 and had depreciable property with an	1. Answer: 100,000 * 20 % = 20,000; no wage limit applicable; because below the threshold for TI
2. Assume Taxpayer has qualified business income and taxable income of $300,000 related to a business that is not a specified service trade or business. The business incurred W-2 wages of $100,000 and had depreciable property with an unadjusted basis of $150,000.	2. Answer: over threshold by $142,500 ($157,500 - $300,000) so wage limitations fully applicable; $300,000 * 20% - $60,000 wages limit: $50,000 [$100,000 * 50%] other limit: $28,750 [$3,750 + $25,000) so limited to $50,000
3. Assume Taxpayer has qualified business income and taxable income of $100,000 related to an accounting sole proprietorship after paying wages of $50,000 to employees.	3. Answer: $100,000 * 20% = $20,000 below threshold SSTB not apply Wage limits not apply
4. Assume Taxpayer has qualified business income and taxable income of $300,000 related to an accounting sole proprietorship after paying wages of $50,000 to employees. Taxpayer has depreciable property with an unadjusted basis of $150,000.	4. Answer: Not eligible; TI more than $50,000 over threshold; thus is an SSTB;
5. Assume Taxpayer has qualified business income and taxable income of $187,500 related to an accounting sole proprietorship after paying wages of $50,000 to employees. Taxpayer has depreciable property with an unadjusted basis of $150,000.	5. Answer: Taxpayer’s deduction is limited to $10,000 Applicable Percentage = 1 - (($187,500 - $157,500)) / $50,000) = 40% Adjusted QBI = $187,500 * 40% = $75,000 20% of Adjusted QBI = 20% * $75,000 = $15,000 Adjusted Wage Base = $50,000 * 40% = $20,000 W-2 Limit - $20,000 * 50% = $10,000 Adjusted Property Base = 40% * $150,000 = $60,000 Alternative Limit: ((25% * $20,000) + (2.5% * 60,000)) = $6,500

Example 1

- Assume Taxpayer has qualified business income and taxable income of $100,000 related to a business that is *not* a specified service trade or business. The business incurred W-2 wages of $50,000 and had depreciable property with an unadjusted basis of $150,000.

Example 2

- Assume Taxpayer has qualified business income and taxable income of $300,000 related to a business that is *not* a specified service trade or business. The business incurred W-2 wages of $100,000 and had depreciable property with an unadjusted basis of $150,000.

Example 3

- Assume Taxpayer has qualified business income and taxable income of $100,000 related to an accounting sole proprietorship after paying wages of $50,000 to employees.

Example 4

- Assume Taxpayer has qualified business income and taxable income of $300,000 related to an accounting sole proprietorship after paying wages of $50,000 to employees. Taxpayer has depreciable property with an unadjusted basis of $150,000.

Example 5

- Assume Taxpayer has qualified business income and taxable income of $187,500 related to an accounting sole proprietorship after paying wages of $50,000 to employees. Taxpayer has depreciable property with an unadjusted basis of $150,000.

Example 5

- Applicable Percentage = 1 - (($187,500 - $157,500)) / $50,000) = 40%
- Adjusted QBI = $187,500 * 40% = $75,000
- 20% of Adjusted QBI = 20% * $75,000 = $15,000
- Adjusted Wage Base = $50,000 * 40% = $20,000
  – W-2 Limit - $20,000 * 50% = $10,000
- Adjusted Property Base = 40% * $150,000 = $60,000
  – Alternative Limit: ((25% * $20,000) + (2.5% * 60,000)) = $6,500

Example 6

- H and W file a joint return reporting taxable income of $375,000.
- W has a qualified trade or business that is not a specified service business. 20 percent of the QBI with respect to the business is $15,000.
- W's share of wages paid by the business is $20,000. 50 percent of the W-2 Wages with respect to the business is $10,000.

Example 6

- (($375,000 - $315,000) / $100,000 = 60%
- 60% * ($15,000 - $10,000) = $3,000
- $15,000 - $3,000 = $12,000

Tax Reform
Section C

C.8. – LIMITATION ON LOSSES FOR TAXPAYERS OTHER THAN CORPORATIONS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Loss limitation rules applicable to individuals **Passive loss rules** The passive loss rules limit deductions and credits from passive trade or business activities. The passive loss rules apply to individuals, estates and trusts, and closely held corporations. A passive activity for this purpose is a trade or business activity in which the taxpayer owns an interest, but in which the taxpayer does not materially participate. A taxpayer is treated as materially participating in an activity only if the taxpayer is involved in the operation of the activity on a basis that is regular, continuous, and substantial. Deductions attributable to passive activities, to the extent they exceed income from passive activities, generally may not be deducted against other income. Deductions and credits that are suspended under these rules are carried forward and treated as deductions and credits from passive activities in the next year. The suspended losses from a passive activity are allowed in full when a taxpayer makes a taxable disposition of his entire interest in the passive activity to an unrelated person. **Excess farm loss rules** A limitation on excess farm losses applies to taxpayers other than C corporations. If a taxpayer other than a C corporation receives an applicable subsidy for the taxable year, the amount of the excess farm loss is not allowed for the taxable year, and is carried forward and treated as a deduction attributable to farming businesses in the next taxable year. An excess farm loss for a taxable year means the excess of aggregate deductions that are attributable to farming businesses over the sum of aggregate gross income or gain attributable to	1. **Limitation.** For taxable years beginning after December 31, 2017 and before January 1, 2026, excess business losses of a taxpayer other than a corporation are not allowed for the taxable year.[1] Such losses are carried forward and treated as part of the taxpayer's net operating loss ("NOL") carryforward in subsequent taxable years.[2] NOL carryovers generally are allowed for a taxable year up to the lesser of the carryover amount or 80 percent of taxable income determined without regard to the deduction for NOLs.[3] 2. **Excess Business Loss.** An excess business loss for the taxable year is the excess of aggregate deductions of the taxpayer attributable to trades or businesses of the taxpayer (determined without regard to the limitation of the provision), over the sum of aggregate gross income or gain of the taxpayer plus a threshold amount. The threshold amount for a taxable year is $250,000 (or twice the otherwise applicable threshold amount in the case of a joint return).[4] The threshold amount is indexed for inflation.[5] 3. **Application to Partnerships and S Corporations.** In the case of a partnership or S corporation, the provision applies at the partner or shareholder level.[6] Each partner's distributive share and each S corporation shareholder's pro rata share of items of income, gain, deduction, or loss of the partnership or S corporation for trades or businesses attributable to the partnership or S corporation are taken into account in applying the limitation under the provision for the taxable year of the partner or S corporation shareholder.[7]	The provision is effective for taxable years beginning after December 31, 2017.	§ 461(L)

C.8. – LIMITATION ON LOSSES FOR TAXPAYERS OTHER THAN CORPORATIONS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
farming businesses plus the threshold amount. The threshold amount is the greater of (1) $300,000 ($150,000 for married individuals filing separately), or (2) for the five-consecutive-year period preceding the taxable year, the excess of the aggregate gross income or gain attributable to the taxpayer's farming businesses over the aggregate deductions attributable to the taxpayer's farming businesses.	**4. Regulatory Authority.** Regulatory authority is also provided to require any additional reporting as the Secretary determines is appropriate to carry out the purposes of the provision. **5. Coordination with Passive Loss Rules.** The provision applies after the application of the passive loss rules.[8] **6. Suspension of Excess Farm Loss Limitation.** For taxable years beginning after December 31, 2017 and before January 1, 2026, the present-law limitation relating to excess farm losses does not apply.[9] [1] I.R.C. § 461(l)(1)(B). [2] I.R.C. § 461(l)(2). [3] I.R.C. § 172(a)(2). [4] I.R.C. § 461(l)(3)(A). [5] I.R.C. § 461(l)(3)(B). [6] I.R.C. § 461(l)(4)(A). [7] I.R.C. § 461(l)(4)(B). [8] I.R.C. § 461(l)(6). [9] I.R.C. § 461(1)A). [10] Act Sec. 11012(b).	For taxable years beginning after December 31, 2017 and before January 1, 2026, the present-law limitation relating to excess farm losses does not apply. The provision is effective for taxable years beginning after December 31, 2017.[10]	§ 461(L)

C.18. – SUSPENSION OF OVERALL LIMITATION ON ITEMIZED DEDUCTIONS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
The total amount of most otherwise allowable itemized deductions (other than the deductions for medical expenses, investment interest and casualty, theft or gambling losses) is limited for certain upper-income taxpayers. All other limitations applicable to such deductions (such as the separate floors) are first applied and, then, the otherwise allowable total amount of itemized deductions is reduced by three percent of the amount by which the taxpayer's adjusted gross income exceeds a threshold amount. For 2017, the threshold amounts are $261,500 for single taxpayers, $287,650 for heads of household, $313,800 for married couples filing jointly, and $156,900 for married taxpayers filing separately. These threshold amounts are indexed for inflation. The otherwise allowable itemized deductions may not be reduced by more than 80 percent by reason of the overall limit on itemized deductions.	**Suspension of Overall Limitation on Itemized Deductions.** For tax year beginning after December 31, 2017, and before January 1, 2026, the Act suspends the overall limitation on itemized deductions.[1] The suspension of the overall limitation on itemized deductions does not apply to taxable years beginning after December 31, 2025.[2] [1] I.R.C. § 68(f). [2] I.R.C. § 68(f). [3] Act Sec. 11046(b).	The provision is effective for taxable years beginning after December 31, 2017.[3]	§ 68

Tax Reform
Section D

D.2. – MODIFICATION OF DEDUCTION FOR TAXES NOT PAID OR ACCRUED IN A TRADE OR BUSINESS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Individuals are permitted a deduction for certain taxes paid or accrued, whether or not incurred in a taxpayer's trade or business. These taxes are: (i) State and local real and foreign property taxes; (ii) State and local personal property taxes; (iii) State, local, and foreign income, war profits, and excess profits taxes. At the election of the taxpayer, an itemized deduction may be taken for State and local general sales taxes in lieu of the itemized deduction for State and local income taxes. Property taxes may be allowed as a deduction in computing adjusted gross income if incurred in connection with property used in a trade or business; otherwise they are an itemized deduction. In the case of State and local income taxes, the deduction is an itemized deduction notwithstanding that the tax may be imposed on profits from a trade or business. Individuals also are permitted a deduction for Federal and State generation skipping transfer tax ("GST tax") imposed on certain income distributions that are included in the gross income of the distributee. In determining a taxpayer's alternative minimum taxable income, no itemized deduction for property, income, or sales tax is allowed.	**1. Effect of Frozen IRC Definitions in Many State Income Tax Regimes**. **a. Many State Income Tax Calculations Will Not Conform With 2017 Federal Changes.** It is critical to understanding how federal tax reform would impact state tax calculations and revenues is generally referred to as "IRC conformity." Most states conform many, though rarely all, sections of their state income tax codes to the IRC. This reduces compliance costs for individuals and businesses. According to a Tax Foundation survey,[1] no state conforms to the IRC in all respects, but most conform to some extent. **b. Frozen or Rolling IRC Conformity.** States conform on either a frozen[2] or rolling[3] basis. Frozen conformity means conforming to the IRC as of a specific date, such as January 1, 2007.[4] Rolling conformity means adopting IRC changes as they occur. Approximately one-half of the states have frozen conformity and about one-half generally adopt changes on rolling basis. Among the states with static conformity, the dates of conformity vary widely. Massachusetts conforms to the IRC as of 2005. Many other states conform as of 2016. So, for example, states that conform to the IRC as of January 1, 2007 or January 1, 2016 will not automatically incorporate the new expanded definitions for Section 179 property. Individuals and companies in frozen IRC states will have to make state income tax calculations based on prior versions of the IRC.	The provision is effective for taxable years beginning after December 31, 2017.	§ 164

D.2. – MODIFICATION OF DEDUCTION FOR TAXES NOT PAID OR ACCRUED IN A TRADE OR BUSINESS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	2. Most Sales and Use Taxes and Property Taxes Imposed Directly on An Active Trade or Business Should Generally Remain Deductible. The Conference Agreement provides that in the case of an individual, state, local, and foreign ***property*** taxes and State and *local* ***sales*** taxes are allowed as a deduction only when paid or accrued in carrying on a trade or business, or an activity described in IRC Section 212 (relating to expenses for the production of income). Therefore, state, local, and foreign ***property*** taxes, and ***sales*** taxes, that are presently deductible in computing income on an individual's Schedule C, Schedule E, or Schedule F on such individual's tax return remain deductible. An individual may deduct property taxes only if these taxes were imposed on business assets (such as residential rental property). It appears that the deduction for sales tax and property tax imposed on an active trade or business will still be allowed to reduce a partner's or LLC members net distributive income. Further study will be needed to determine if an entity level business tax, such as the Texas franchise tax, which is imposed on LLC's and partnerships remains deductible, but it appears that it may remain deductible. **3. New IRC Only Allows Deduction of 100% of State Income Taxes for C Corps.** Under the Conference Agreement, in the case of an individual, state and local income, taxes are not allowable as a deduction above $10,000 ($5,000 for married taxpayer filing a separate return) for the aggregate of (i) State and local property taxes not paid or accrued in carrying on a trade or business, or an activity described in section 212, and (ii) state and local income taxes, paid or accrued in the taxable year.		§ 164

D.2. – MODIFICATION OF DEDUCTION FOR TAXES NOT PAID OR ACCRUED IN A TRADE OR BUSINESS

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	[1] https://taxfoundation.org/federal-tax-reform-the-impact-on-states/ [2] Approximately 18 states have a frozen conformity date drafted into their state income tax laws. [3] Approximately 20 states have rolling conformity. [4] *See e.g.,* Tex. Tax Code Section 171.0001(9) (“"Internal Revenue Code" means the Internal Revenue Code of 1986 in effect for the federal tax year beginning on January 1, 2007, not including any changes made by federal law after that date, and any regulations adopted under that code applicable to that period.”)		§ 164

D.6. - REPEAL OF CERTAIN MISCELLANEOUS ITEMIZED DEDUCTIONS SUBJECT TO THE TWO-PERCENT FLOOR

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Individuals may claim itemized deductions for certain miscellaneous expenses. Certain of these expenses are not deductible unless, in aggregate, they exceed two percent of the taxpayer's adjusted gross income ("AGI"). The deductions described below are subject to the aggregate two-percent floor. **<u>Expenses for the production or collection of income</u>** Individuals may deduct all ordinary and necessary expenses paid or incurred during the taxable year for the production or collection of income. Present law and IRS guidance provide examples of items that may be deducted under this provision. This non-exhaustive list includes: • Appraisal fees for a casualty loss or charitable contribution; • Casualty and theft losses from property used in performing services as an employee; • Clerical help and office rent in caring for investments; • Depreciation on home computers used for investments; • Excess deductions (including administrative expenses) allowed a beneficiary on termination of an estate or trust; • Fees to collect interest and dividends; • Hobby expenses, but generally not more than hobby income; • Indirect miscellaneous deductions from pass-through entities; • Investment fees and expenses;	**1. In General.** The provision suspends all miscellaneous itemized deductions that are subject to the two-percent floor under present law.[1] Thus, under the provision, taxpayers may not claim Miscellaneous Itemized Deductions[2] as itemized deductions for the taxable years to which the suspension applies. **2. Applicable Suspension Period.** The provision applies for taxable years beginning after December 31, 2017 and does not apply for taxable years beginning after December 31, 2025.[3] [1] I.R.C. § 67(g). [2] I.R.C. § 67(b). [3] I.R.C. § 67(g). [4] Tax Cuts and Jobs Act § 11046(b).	The provision is effective for taxable years beginning after December 31, 2017.[4]	§ 62 § 67 § 212

D.6. - REPEAL OF CERTAIN MISCELLANEOUS ITEMIZED DEDUCTIONS SUBJECT TO THE TWO-PERCENT FLOOR

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
• Loss on deposits in an insolvent or bankrupt financial institution; • Loss on traditional IRAs or Roth IRAs, when all amounts have been distributed; • Repayments of income; • Safe deposit box rental fees, except for storing jewelry and other personal effects; • Service charges on dividend reinvestment plans; and • Trustee's fees for an IRA, if separately billed and paid. **<u>Tax preparation expenses</u>** For regular income tax purposes, individuals are allowed an itemized deduction for expenses for the production of income. These expenses are defined as ordinary and necessary expenses paid or incurred in a taxable year: (1) for the production or collection of income; (2) for the management, conservation, or maintenance of property held for the production of income; or (3) in connection with the determination, collection, or refund of any tax. **<u>Unreimbursed expenses attributable to the trade or business of being an employee</u>** In general, unreimbursed business expenses incurred by an employee are deductible, but only as an itemized deduction and only to the extent the expenses exceed two percent of adjusted gross income. Present law and IRS guidance provide examples of items that may be deducted under this provision. This non-exhaustive list includes: • Business bad debt of an employee; • Business liability insurance premiums;			§ 62 § 67 § 212

D.6. - REPEAL OF CERTAIN MISCELLANEOUS ITEMIZED DEDUCTIONS SUBJECT TO THE TWO-PERCENT FLOOR

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
• Damages paid to a former employer for breach of an employment contract; • Depreciation on a computer a taxpayer's employer requires him to use in his work; • Dues to a chamber of commerce if membership helps the taxpayer perform his job; • Dues to professional societies; • Educator expenses; • Home office or part of a taxpayer's home used regularly and exclusively in the taxpayer's work; • Job search expenses in the taxpayer's present occupation; • Laboratory breakage fees; • Legal fees related to the taxpayer's job; • Licenses and regulatory fees; • Malpractice insurance premiums; • Medical examinations required by an employer; • Occupational taxes; • Passport fees for a business trip; • Repayment of an income aid payment received under an employer's plan; • Research expenses of a college professor; • Rural mail carriers' vehicle expenses; • Subscriptions to professional journals and trade magazines related to the taxpayer's work; • Tools and supplies used in the taxpayer's work; • Purchase of travel, transportation, meals, entertainment, gifts, and local lodging related to the taxpayer's work; • Union dues and expenses;			§ 62 § 67 § 212

D.6. - REPEAL OF CERTAIN MISCELLANEOUS ITEMIZED DEDUCTIONS SUBJECT TO THE TWO-PERCENT FLOOR

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
• Work clothes and uniforms if required and not suitable for everyday use; and • Work-related education. **Other miscellaneous itemized deductions subject to the two-percent floor** Other miscellaneous itemized deductions subject to the two-percent floor include: • Repayments of income received under a claim of right (only subject to the two- percent floor if less than $3,000); • Repayments of Social Security benefits; and • The share of deductible investment expenses from pass-through entities.			§ 62 § 67 § 212

Tax Reform
Section F

F. - MODIFICATIONS TO ESTATE, GIFT, AND GENERATION-SKIPPING TRANSFERS TAXES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
<u>Transfer Tax Basic Exclusion Amount – Unified Credit</u> **<u>Estate and Gift Taxes</u>**: A unified credit is available with respect to taxable transfers by gift and at death. The unified credit offsets tax, computed using the applicable estate and gift tax rates, on a specified amount of transfers, referred to as the applicable exclusion amount, which is the "basic exclusion amount" plus, in the case of a surviving spouse, any of the pre-deceased spouse's unused basic exclusion amount that has been elected for use by the surviving spouse (exemption portability). The basic exclusion amount was set at $5 million for 2011, indexed for inflation for later years. For 2017, the inflation-indexed basic exclusion amount is $5.49 million. Any applicable exclusion amount used during life to offset taxable gifts in effect reduces the amount of the applicable exclusion amount that remains at death to offset the value of a decedent's estate.	The Act (§11061) increases the basic exclusion amount [is increased] to $5 million to $10 million (indexed for inflation occurring after 2011), using the new "chained CPI indexing approach). (the legislative history refers to this change as doubling the "estate and gift tax exemption," but it also doubles the GST exemption because §2631j(c) provides that the GST exemption is "equal to the basic exclusion amount under section 2010(c). Since any applicable gift exclusion amount used during life to offset taxable gifts in effect reduces the applicable estate tax exclusion amount that remains at death, there is [given the sun setting of the increased exclusion amount under the Act and the resulting return to the $5 million (indexed for inflation) basic exclusion amount under the pre-Reform law] the possibility of an individual's using more gift tax exclusion amount (for taxable gifts made after 2017 and before 2026) than the $5 million (indexed for inflation) estate exclusion that is slated to return in 2026. This gives rise to the question of whether the excess gift exclusion amount used over the $5 million estate tax exclusion is to be somehow "clawed back" in computing the donor's estate tax liability. Under §11061 of the Act, a new I.R.C. §2001(g)(2) is added directing the Treasury to prescribe regulations as may be necessary or appropriate any difference in the basic exclusion amount at the time of a gift and at the time of death.	Estates of decedents dying, and gifts made after 2017 and before 2026.	§ 2010(c)(3)

F. - MODIFICATIONS TO ESTATE, GIFT, AND GENERATION-SKIPPING TRANSFERS TAXES

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
<u>Generation-skipping Transfer Tax</u>: The generation-skipping transfer tax is imposed on cumulative generation- skipping transfers in excess of the generation-skipping transfer tax exemption amount in effect for the year of the transfer. The generation-skipping transfer tax exemption for a given year is equal to the estate tax exemption amount in effect for that year ($5.49 million for 2017).	Because I.R.C. §2631(c) provides that the GST exemption equal to the basic exclusion amount under I.R.C. §2010(c), the increase in the estate tax basic exclusion amount serves to increase, in like manner, the GST exemption.	Generation-skipping transfers made after 2017 and before 2026.	§2631(c), as affected by §2010(c)(3)
<u>Indexing for the Basic Exclusion Amount for Inflation</u>. Under the I.R.C., many parameters of the tax system (including the estate and gift tax basic exclusion amount and the GST tax exemption) are adjusted for inflation to protect taxpayers from the effects of rising prices. Under pre-reform law, most of the adjustments are based on annual changes in the level of the Consumer Price Index for All Urban Consumers ("CPI-U"). The CPI-U is an index that measures prices paid by typical urban consumers on a broad range of products, and is developed and published by the Department of Labor.	The Act (§11002) applies a different measure of inflation for indexing the affected parameters of the tax system (including the estate and gift tax basic exclusion and the GST exemption. Rather than using the CPI-U as the measure, the "Chained Consumer Price Index for All Urban Consumers" ("C-CPI-U") is to be used. The C-CPI-U is a measure of the average change over time in prices paid by urban consumers. It is developed and published by the Department of Labor, but differs from the CPI-U in accounting for the ability of individuals to alter their consumption patterns in response to relative price changes, and it accomplishes this by allowing for consumer substitution between item categories in the market basket of consumer goods and services that make up the index (while the CPI-U only allows for modest substitution within item categories).	All taxable years beginning after December 31, 2017. The change in the measure of indexing for inflation is permanent.	§1(f)

Tax Reform
Section G

G. ALTERNATIVE MINIMUM TAX

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Individual alternative minimum tax **In general** An alternative minimum tax ("AMT") is imposed on an individual, estate, or trust in an amount by which the tentative minimum tax exceeds the regular income tax for the taxable year. For taxable years beginning in 2017, the tentative minimum tax is the sum of (1) 26 percent of so much of the taxable excess as does not exceed $187,800 ($93,900 in the case of a married individual filing a separate return) and (2) 28 percent of the remaining taxable excess. The breakpoints are indexed for inflation. The taxable excess is so much of the alternative minimum taxable income ("AMTI") as exceeds the exemption amount. The maximum tax rates on net capital gain and dividends used in computing the regular tax are used in computing the tentative minimum tax. AMTI is the taxable income adjusted to take account of specified tax preferences and adjustments. The exemption amounts for taxable years beginning in 2017 are: (1) $84,500 in the case of married individuals filing a joint return and surviving spouses; (2) $54,300 in the case of other unmarried individuals; (3) $42,250 in the case of married individuals filing separate returns; and (4) $24,100 in the case of an estate or trust. For taxable years beginning in 2017, the exemption amounts are phased out by an amount equal to 25 percent of the amount by which the individual's AMTI exceeds (1) $160,900 in the case of married individuals filing a joint return and surviving spouses, (2) $120,700 in the case of other unmarried individuals, and (3) $80,450 in the case of married individuals filing separate returns or an estate or a trust. The amounts are indexed for inflation.	**1. Individual AMT.** The Act temporarily increases both the exemption amount and the exemption amount phaseout thresholds for the individual Alternative Minimum Tax (AMT). **a. Increased Exemption.** Under the Act, for taxable years beginning after December 31, 2017, and beginning before January 1, 2026, the AMT exemption amount is increased to $109,400 for married taxpayers filing a joint return[1] (half this amount for married taxpayers filing a separate return[2]), and $70,300 for all other taxpayers[3] (other than estates and trusts[4]). **b. Increased Exemption Phaseout.** The phaseout thresholds for the exemption are increased to $1,000,000 for married taxpayers filing a joint return,[5] and $500,000 for all other taxpayers[6] (other than estates and trusts[7]). These amounts are indexed for inflation.[8] **2. Corporate AMT** **a. Repeal of Corporate AMT.** The Act repeals the corporate alternative minimum tax.[9] **b. Corporate AMT Credit.** The Act continues to allow the AMT credit to offset the regular tax liability for any taxable year of a corporation.[10] In addition, the AMT credit is refundable for any taxable year beginning after 2017 and before 2022[11] in an amount equal to 50 percent (100 percent in the case of taxable years beginning in 2021) of the excess of the total minimum tax credit for the taxable year over the amount of the credit allowable for the year against regular tax liability.[12]	The provisions of the Act are effective for taxable years beginning after December 31, 2017.[13]	§ 53 § 55-59

G. ALTERNATIVE MINIMUM TAX

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
AMTI is the taxpayer's taxable income increased by certain preference items and adjusted by determining the tax treatment of certain items in a manner that negates the deferral of income resulting from the regular tax treatment of those items. **<u>Preference items in computing AMTI</u>** The minimum tax preference items are: 1. The excess of the deduction for percentage depletion over the adjusted basis of each mineral property (other than oil and gas properties) at the end of the taxable year. 2. The amount by which excess intangible drilling costs (i.e., expenses in excess the amount that would have been allowable if amortized over a 10-year period) exceed 65 percent of the net income from oil, gas, and geothermal properties. This preference applies to independent producers only to the extent it reduces the producer's AMTI (determined without regard to this preference and the net operating loss deduction) by more than 40 percent. 3. Tax-exempt interest income on private activity bonds (other than qualified 501(c)(3) bonds, certain housing bonds, and bonds issued in 2009 and 2010) issued after August 7, 1986. 4. Accelerated depreciation or amortization on certain property placed in service before January 1, 1987. 5. Seven percent of the amount excluded from income under section 1202 (relating to gains on the sale of certain small business stock). In addition, losses from any tax shelter farm activity or passive activities are not taken into account in computing AMTI.	[1] I.R.C. § 55(d)(4)(A)(i)(I); *see id.* § 55(d)(1)(A). [2] I.R.C. § 55(d)(1)(C). [3] I.R.C. § 55(d)(4)(A)(i)(II); *see id.* § 55(d)(1)(B). [4] *See* I.R.C. § 55(d)(1)(D). [5] I.R.C. § 55(d)(4)(A)(ii)(I); *see id.* § 55(d)(2)(A), (1)(A). [6] *See* I.R.C. § 55(d)(4)(A)(ii)(II); *see id.* § 55(d)(2)(B), (1)(B). [7] I.R.C. § 55(d)(4)(A)(ii)(III); *see id.* § 55(d)(1)(D). [8] I.R.C. § 55(d)(4)(B). [9] *See* I.R.C. § 55(a) (applying the AMT to taxpayers "other than a corporation."). [10] *See* I.R.C. § 53(a). [11] *See* I.R.C. § 53(e)(1). [12] I.R.C. § 53(e)(2). [13] Tax Cuts and Jobs Act §§ 12001(c), 12002(d), 12003(b).		§ 53 § 55-59

G. ALTERNATIVE MINIMUM TAX

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Adjustments in computing AMTI The adjustments that individuals must make to compute AMTI are: 1. Depreciation on property placed in service after 1986 and before January 1, 1999, is computed by using the generally longer class lives prescribed by the alternative depreciation system of section 168(g) and either (a) the straight-line method in the case of property subject to the straight-line method under the regular tax or (b) the 150-percent declining balance method in the case of other property. Depreciation on property placed in service after December 31, 1998, is computed by using the regular tax recovery periods and the AMT methods described in the previous sentence. Depreciation on property acquired after September 10, 2001, which is allowed an additional allowance under section 168(k) for the regular tax is computed without regard to any AMT adjustments. 2. Mining exploration and development costs are capitalized and amortized over a 10- year period. 3. Taxable income from a long-term contract (other than a home construction contract) is computed using the percentage of completion method of accounting. 4. Depreciation on property placed in service after 1986 and before January 1, 1999, is computed by using the generally longer class lives prescribed by the alternative depreciation system of section 168(g) and either (a) the straight-line method in the case of property subject to the straight-line method under the regular tax or (b) the 150-percent declining balance method in the case of other property.			§ 53 § 55-59

G. ALTERNATIVE MINIMUM TAX

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Depreciation on property placed in service after December 31, 1998, is computed by using the regular tax recovery periods and the AMT methods described in the previous sentence. Depreciation on property acquired after September 10, 2001, which is allowed an additional allowance under section 168(k) for the regular tax is computed without regard to any AMT adjustments. 5. Mining exploration and development costs are capitalized and amortized over a 10- year period. 6. Taxable income from a long-term contract (other than a home construction contract) is computed using the percentage of completion method of accounting. 7. The amortization deduction allowed for pollution control facilities placed in service before January 1, 1999 (generally determined using 60-month amortization for a portion of the cost of the facility under the regular tax), is calculated under the alternative depreciation system (generally, using longer class lives and the straight- line method). The amortization deduction allowed for pollution control facilities placed in service after December 31, 1998, is calculated using the regular tax recovery periods and the straight-line method. 8. Miscellaneous itemized deductions are not allowed. 9. Itemized deductions for State, local, and foreign real property taxes; State and local personal property taxes; State, local, and foreign income, war profits, and excess profits taxes; and State and local sales taxes are not allowed.			§ 53 § 55-59

G. ALTERNATIVE MINIMUM TAX

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
10. Medical expenses are allowed only to the extent they exceed ten percent of the taxpayer's adjusted gross income. 11. Deductions for interest on home equity loans are not allowed. 12. The standard deduction and the deduction for personal exemptions are not allowed. 13. The amount allowable as a deduction for circulation expenditures is capitalized and amortized over a three-year period. 14. The amount allowable as a deduction for research and experimentation expenditures from passive activities is capitalized and amortized over a 10-year period. 15. The regular tax rules relating to incentive stock options do not apply. **<u>Other rules</u>** The taxpayer's net operating loss deduction generally cannot reduce the taxpayer's AMTI by more than 90 percent of the AMTI (determined without the net operating loss deduction). The alternative minimum tax foreign tax credit reduces the tentative minimum tax. The various nonrefundable business credits allowed under the regular tax generally are not allowed against the AMT. Certain exceptions apply. If an individual is subject to AMT in any year, the amount of tax exceeding the taxpayer's regular tax liability is allowed as a credit (the "AMT credit") in any subsequent taxable year to the extent the taxpayer's regular tax liability exceeds his or her tentative			§ 53 § 55-59

G. ALTERNATIVE MINIMUM TAX

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
minimum tax liability in such subsequent year. The AMT credit is allowed only to the extent that the taxpayer's AMT liability is the result of adjustments that are timing in nature. The individual AMT adjustments relating to itemized deductions and personal exemptions are not timing in nature, and no minimum tax credit is allowed with respect to these items. An individual may elect to write off certain expenditures paid or incurred with respect of circulation expenses, research and experimental expenses, intangible drilling and development expenditures, development expenditures, and mining exploration expenditures over a specified period (three years in the case of circulation expenses, 60 months in the case of intangible drilling and development expenditures, and 10 years in case of other expenditures). The election applies for purposes of both the regular tax and the alternative minimum tax. **Corporate alternative minimum tax** **In general** An AMT is also imposed on a corporation to the extent the corporation's tentative minimum tax exceeds its regular tax. This tentative minimum tax is computed at the rate of 20 percent on the AMTI in excess of a $40,000 exemption amount that phases out. The exemption amount is phased out by an amount equal to 25 percent of the amount that the corporation's AMTI exceeds $150,000. AMTI is the taxpayer's taxable income increased by certain preference items and adjusted by determining the tax treatment of certain items in a manner that negates the deferral of income resulting from the regular tax treatment of those items.			§ 53 § 55-59

G. ALTERNATIVE MINIMUM TAX

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
A corporation with average gross receipts of less than $7.5 million for the prior three taxable years is exempt from the corporate minimum tax. The $7.5 million threshold is reduced to $5 million for the corporation's first three-taxable year period. **<u>Preference items in computing AMTI</u>** The corporate minimum tax preference items are: 1. The excess of the deduction for percentage depletion over the adjusted basis of the property at the end of the taxable year. This preference does not apply to percentage depletion allowed with respect to oil and gas properties. 2. The amount by which excess intangible drilling costs arising in the taxable year exceed 65 percent of the net income from oil, gas, and geothermal properties. This preference does not apply to an independent producer to the extent the preference would not reduce the producer's AMTI by more than 40 percent. 3. Tax-exempt interest income on private activity bonds (other than qualified 501(c)(3) bonds, certain housing bonds, and bonds issued in 2009 and 2010) issued after August 7, 1986. 4. Accelerated depreciation or amortization on certain property placed in service before January 1, 1987. **<u>Adjustments in computing AMTI</u>** The adjustments that corporations must make in computing AMTI are: 1. Depreciation on property placed in service after 1986 and before January 1, 1999, must be computed by using the generally longer class lives prescribed by the alternative depreciation system of section 168(g) and either (a) the straight-line method			§ 53 § 55-59

G. ALTERNATIVE MINIMUM TAX

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
in the case of property subject to the straight-line method under the regular tax or (b) the 150-percent declining balance method in the case of other property. Depreciation on property placed in service after December 31, 1998, is computed by using the regular tax recovery periods and the AMT methods described in the previous sentence. Depreciation on property which is allowed "bonus depreciation" for the regular tax is computed without regard to any AMT adjustments. 2. Mining exploration and development costs must be capitalized and amortized over a 10-year period. 3. Taxable income from a long-term contract (other than a home construction contract) must be computed using the percentage of completion method of accounting. 4. The amortization deduction allowed for pollution control facilities placed in service before January 1, 1999 (generally determined using 60-month amortization for a portion of the cost of the facility under the regular tax), must be calculated under the alternative depreciation system (generally, using longer class lives and the straight-line method). The amortization deduction allowed for pollution control facilities placed in service after December 31, 1998, is calculated using the regular tax recovery periods and the straight-line method. 5. The special rules applicable to Merchant Marine construction funds are not applicable. 6. The special deduction allowable under section 833(b) for Blue Cross and Blue Shield organizations is not allowed. 7. The adjusted current earnings adjustment applies, as described below.			§ 53 § 55-59

G. ALTERNATIVE MINIMUM TAX

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
<u>Adjusted current earning ("ACE") adjustment</u> The adjusted current earnings adjustment is the amount equal to 75 percent of the amount by which the adjusted current earnings of a corporation exceed its AMTI (determined without the ACE adjustment and the alternative tax net operating loss deduction). In determining ACE the following rules apply: 1. For property placed in service before 1994, depreciation generally is determined using the straight-line method and the class life determined under the alternative depreciation system. 2. Amounts excluded from gross income under the regular tax but included for purposes of determining earnings and profits are generally included in determining ACE. 3. The inside build-up of a life insurance contract is included in ACE (and the related premiums are deductible). 4. Intangible drilling costs of integrated oil companies must be capitalized and amortized over a 60-month period. 5. The regular tax rules of section 173 (allowing circulation expenses to be amortized) and section 248 (allowing organizational expenses to be amortized) do not apply. 6. Inventory must be calculated using the FIFO, rather than LIFO, method. 7. The installment sales method generally may not be used. 8. No loss may be recognized on the exchange of any pool of debt obligations for another pool of debt obligations having substantially the same effective interest rates and maturities.			§ 53 § 55-59

G. ALTERNATIVE MINIMUM TAX

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
9. Depletion (other than for oil and gas properties) must be calculated using the cost, rather than the percentage, method. 10. In certain cases, the assets of a corporation that has undergone an ownership change must be stepped down to their fair market values. **<u>Other rules</u>** The taxpayer's net operating loss carryover generally cannot reduce the taxpayer's AMT liability by more than 90 percent of AMTI determined without this deduction. The various nonrefundable business credits allowed under the regular tax generally are not allowed against the AMT. Certain exceptions apply. If a corporation is subject to AMT in any year, the amount of AMT is allowed as an AMT credit in any subsequent taxable year to the extent the taxpayer's regular tax liability exceeds its tentative minimum tax in the subsequent year. Corporations are allowed to claim a limited amount of AMT credits in lieu of bonus depreciation. A corporation may elect to write off certain expenditures paid or incurred with respect of circulation expenses, research and experimental expenses, intangible drilling and development expenditures, development expenditures, and mining exploration expenditures over a specified period (three years in the case of circulation expenses, 60 months in the case of intangible drilling and development expenditures, and 10 years in case of other expenditures). The election applies for purposes of both the regular tax and the alternative minimum tax.			§ 53 § 55-59

Tax Reform
Section H

H.12. - TAX REPORTING FOR LIFE SETTLEMENT TRANSACTIONS/INSURANCE POLICY CONTRACT BASIS/TRANSFER FOR VALUE

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
An exclusion from Federal income tax is provided for amounts received under a life insurance contract paid by reason of the death of the insured. Under rules known as the transfer for value rules, if a life insurance contract is sold or otherwise transferred for valuable consideration, the amount paid by reason of the death of the insured that is excludible is limited. Under the limitation, the excludable amount may not exceed the sum of (1) the actual value of the consideration paid, and (2) the premiums or other amounts paid by the transferee of the contract. Thus, for example, if a person buys a life insurance contract, and the consideration he pays combined with his subsequent premium payments on the contract are less than the amount of the death benefit he later received under the contract, then the difference is includible in the buyer's income. Exceptions are provided to the limitation on the excludible amount. The limitation on the explicable amount does not apply if (1) the transferee's basis in the contract is determined in whole or in part by reference to the transferor's basis in the contract, or (2) the transfer is to the insured, to a partner of the insured, to a partnership in which the insured is a partner, or to a corporation in which the insured is a shareholder or officer. IRS guidance sets forth more details of the tax treatment of a life insurance policyholder who sells or surrenders the life insurance contract and the tax treatment of other sellers and of buyers of life insurance contracts. The guidance related to the character of taxable amounts (ordinary or capital) and to the taxpayer's basis in the life insurance contract.	**<u>Scope of Transfer for Value Rules</u>** Act §13522 provides that the exceptions to the transfer for value rules do not apply in the case of a transfer of a life insurance contract, or any interest in a life insurance contract, in a "reportable policy sale." A "reportable policy sale" means the acquisition of an interest in a life insurance contract, directly or indirectly, if the acquirer has no substantial family, business, or financial relationship with the insured apart from the acquirer's interest in such life insurance contract. The term "indirectly" applies to the acquisition of an interest in a partnership, trust, or other entity that holds an interest in the life insurance contract.	Applicable to transfers after December 31, 2017	New § 101(a)(3)
	<u>Determination of Basis in Life Insurance Contract</u> Act §13521 provides that in determining the basis of a life insurance or annuity contract, no adjustment is made for mortality, expense, or other reasonable charged incurred under the contract (known as "cost of insurance"). This reverses the position of the IRS in Revenue Ruling 2009-13 that on the sale of a cash value life insurance contract, the insured's (seller') basis is reduced by the cost of insurance.	Applies to transactions entered into after August 25, 2009	§ 1016(a)(1)
	<u>Reporting Requirements with Respect to Life Insurance Contracts - In General</u> Act §§13520 imposes reporting requirements in the case of the purchase of an existing life insurance contract in a "reportable policy sale" (as defined in new I.R.C. sec. 101(a)(3) (*See* Scope of Transfer for Value Rules above) and imposes reporting requirement on the payor in the case of the payment of "reportable death benefit."	Reportable policy sales after 2017 and reportable death benefits after 2017	New § 6050Y

H.12. - TAX REPORTING FOR LIFE SETTLEMENT TRANSACTIONS/INSURANCE POLICY CONTRACT BASIS/TRANSFER FOR VALUE

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
In Revenue Ruling 2009-13, the IRS ruled that income recognized under section 72(e) on surrender to the life insurance company of a life insurance contract with cash value is ordinary income. In the case of sale of a cash value life insurance contract, the IRS ruled that the insured's (seller's) basis is reduced by the cost of insurance, and the gain on sale of the contract is ordinary income to the extent of the amount that would be recognized as ordinary income if the contract were surrendered (the "inside buildup"), and any excess is long-term capital gain. Gain on the sale of a term life insurance contract (without cash surrender value) is long-term capital gain under the ruling. In Revenue ruling 2009-14, the IRS ruled that under the transfer for value rules, a portion of the death benefit received by a buyer of a life insurance contract on the death of the insured is includable as ordinary income. The portion is the excess of the death benefit over the consideration and other amounts (e.g., premiums) paid for the contract. Upon sale of the contract by the purchaser of the contract, the gain is long-term capital gain, and in determining the gain, the basis of the contract is not reduced by the cost of insurance.	Act §13521 sets forth rules for determining the basis of a life insurance or annuity contract. Act §13522 modifies the transfer for value rules in a transfer of an interest in a life insurance contract in a "reportable policy sale." **<u>Reporting Requirements for Acquisitions of Life Insurance Contracts</u>** **<u>Reporting Upon Acquisition of Life Insurance Contract</u>**. The reporting requirement applies to every person who acquires a life insurance contract, or any interest in a life insurance contract, in a "reportable policy sale" during the taxable year. Under the reporting requirement, the buyer is required to file an information return with the IRS that contains the following information: (1) the buyer's name, address, and TIN, (2) the name, address, and TIN of each recipient of a payment in the reportable policy sale, (3) the date of the sale, (4) the name of the issuer of the insurance contract and the contract number, and (5) the amount of each payment. The buyer is also required to furnish a statement to each person (including the issuing insurance company) whose name is required to be included in the information return. The statement furnished to each such person must include the name, address and telephone number of the information contact of the buyer, as well as all of the information required to be included in the formation return; however the statement the buyer provides to any issuer of a life insurance contact is not required to include the amount of the payment or payments for the purchase of the contract.		New § 6050Y

H.12. - TAX REPORTING FOR LIFE SETTLEMENT TRANSACTIONS/INSURANCE POLICY CONTRACT BASIS/TRANSFER FOR VALUE

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	Reporting of Seller's Basis in the Life Insurance Contract. On receipt of the report upon acquisition of a life insurance contract in a reportable sale, or on any notice of the transfer of a life insurance contract to a foreign person, the insurance company issuing the policy is required to file an information return with the IRS that sets forth (1) the name, address, and TIN of the seller or the transferor to a foreign person, (2) the basis of the contract (*i.e.*, the investment in the contract within the meaning of I.R.C. sec. 72(e)(6)), and (3) the policy number of the contract. The insurance company issuing the policy is also required to furnish a statement to each person whose name is required to be included in the information return, such statement to include the name, address, and telephone number of the information contact of the issuing insurance company and all information required to be included in the information return. According to the Conference Committee Report, notice of the transfer of a life insurance contract to a foreign person is intended to include any sort of notice, including information provided for nontax purposes, such as change of address notices for purposes of sending statement or for other purposes, or information relating to loans, premiums, or death benefits with respect to the contract.		New § 6050Y

H.12. - TAX REPORTING FOR LIFE SETTLEMENT TRANSACTIONS/INSURANCE POLICY CONTRACT BASIS/TRANSFER FOR VALUE

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	<u>Reporting With Respect to Reportable Death Benefits</u> When a “reportable death benefit” is paid under a life insurance contract, the payor insurance company is required to file an information return with the IRS. A “reportable death benefit” means an amount paid by reason of the death of the insured under a life insurance contract that has been transferred in a reportable policy sale. The information required to be reported to the IRS includes (1) the name, address, and TIN of the person making the payment, (2) the name, address and TIN of each recipient of a payment, (3) the date of each such payment, (4) the gross amount of the payment, and (5) the payor’s estimate of the buyer’s basis in the contract. A statement is also to be provided to each person whose name is required to be stated in the information return, which is to include the name, address, and telephone number of the information contact of the issuing insurance company and all information required to be included in the information return. **<u>Time and Manner of Reporting</u>** The Secretary of the Treasury is to issue regulations regarding the manner and time of reporting under new I.R.C. sec. 6050Y.		New § 6050Y

H.12. - TAX REPORTING FOR LIFE SETTLEMENT TRANSACTIONS/INSURANCE POLICY CONTRACT BASIS/TRANSFER FOR VALUE

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	Penalties for Failure to File Information Return or Provide Statements The information returns required to be filed with the IRS in connection with a reportable policy sale, the seller's/transferor's basis in a reportable sale or a transfer of a life insurance contract to a foreign person, and the payment of a reportable death benefit are "information return" for purposes of the failure to file information returns penalty under I.R.C. sec. 6721. The statements required to be provided to each person named in such an information return are "payee statements" for purposes of the failure to furnish correct payee statements under I.R.C. sec. 6722. I.R.C. sec. 6047, relating to certain reporting requirements by life insurance companies, does not apply to any information that is required to be reported under new I.R.C. sec. 6050Y.		New § 6050Y

Tax Reform
Exempt Organization

EXEMPT ORGANIZATION TAX REFORM UNRELATED BUSINESS TAXABLE INCOME

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Multiple Trades or Businesses An exempt organization may have revenue from four sources: contributions, gifts,, and grants; trade or business income that is related to its exempt activities (e.g. program service revenue); investment income; and trade or business income that is not related to exempt activities. The Federal income tax exemption generally extends to the first three categories and does not extend to an organization's unrelated trade or business income. (in some cases, investment income of an organization is taxed as if it were unrelated trade or business income). The unrelated business income tax ("UBIT") generally applies to income derived from a trade or business regularly carried on by the organization that is not substantially related to the performance of the organization's tax-exempt functions. An organization that is subject to UBIT and that has $1,000 or more of gross unrelated business taxable income must report that income on form 990-T. Most exempt organizations may operate an unrelated trade or business as long as the organization remains primarily engaged in activities that further its exempt purposes. An organization may engage in a substantial amount of unrelated business activity without jeopardizing exempt statues, except that a section 501(c)(3) charitable organization may not operate an unrelated trade or organization may not operate an unrelated trade or business as a substantial part of its activities, but must be an insubstantial part.	Under §13702 of the Act, for an organization with more than one unrelated trade or business, the unrelated business taxable income is to be first computed separately with respect to each trade or business and without regard to the specific deduction generally allowed under I.R.C. sec. 512(b)(12). The organization's unrelated business taxable income for a taxable year is the sum of the amounts (not less than zero) computed for each separate unrelated trade or business, less the specific deduction allowed under I.R.C. sec. 512(b)(12). A net operating loss deduction is allowed only with respect to a trade or business from which the loss arose. Accordingly, a deduction from one trade or business for a taxable year may not be used to offset income from a different unrelated trade or business for the same taxable year. The provision generally does not, however, prevent an organization from using a deduction from one taxable year to offset income from the same unrelated trade or business activity in another taxable year, where appropriate.	Applicable to taxable years beginning after December 31, 2017, except that if any net operating loss arises before January 1, 2018 is carried over to a taxable year beginning on or after that date, the $1,000 specific deduction does not apply to that loss and the unrelated business taxable income of the organization is generally to be reduced by the amount of net operating loss.	New § 512(a)(6)

EXEMPT ORGANIZATION TAX REFORM
UNRELATED BUSINESS TAXABLE INCOME

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
Most exempt organizations are subject to the tax on unrelated business income, and there are some types of income that are specifically exempt from unrelated business taxable income, such as dividends, interest, royalties and certain rents. Other exemptions from UBIT are provided, such as (but not limited to) income for activities in which substantially all the work is performed by volunteers, for income from the sale of donated goods, and for certain activities carried on for the convenience of members, students, patients, officers, or employees of a charitable organization. An organization determines its unrelated business taxable income by subtracting from its gross unrelated business income deductions directly connected with the unrelated trade or business. Under regulations, in determining the unrelated business taxable income, an organization that operates multiple unrelated trades or businesses aggregates income from all such activities and subtracts from the aggregate gross income the aggregate of deductions. As a result, the organization may use a deduction from one unrelated trade or business to offset income from another, thereby reducing total unrelated business taxable income. In computing unrelated business taxable income, an exempt organization may take a specific deduction of $1,000. This specific deduction may not be used to create a net operating loss that will be carried back or forward to another year.			New § 512(a)(6)

EXEMPT ORGANIZATION TAX REFORM
UNRELATED BUSINESS TAXABLE INCOME

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
<u>Unrelated Business Taxable Income Increased by Amount of Certain Fringe Benefits Expenses for Which Deduction is Disallowed</u> Currently, unrelated business taxable income does not include any expenses paid or incurred by a tax exempt organization for qualified transportation fringe benefit, a parking facility used in connection with qualified parting, or any on-premises athletic facility.	Under §13703 of the Act, unrelated business taxable income includes any expenses paid or incurred by a tax exempt organization for qualified transportation fringe benefits (as defined in I.R.C. sec. 132(f)), a parking facility used in connection with qualified parking (as defined in I.R.C. sec. 132(f)(5)(c), or any on-premises athletic facility (as defined in I.R.C. sec. 132(j)(4)(B), provided such amounts are not deductible under I.R.C. sec. 274.	Amounts paid or incurred after December 31, 2017	New § 512(a)(7)

Tax Reform International Tax Provisions

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Controlled Foreign Corporation A CFC generally is defined as any foreign corporation if U.S. persons own (directly, indirectly, or constructively) more than 50 percent of the corporation's stock (measured by vote or value), taking into account only those U.S. persons that are within the meaning of the term "United States shareholder," which refers only to those U.S. persons who own at least 10 percent of the stock (measured by vote only). **Investments in U.S. property** The 10-percent U.S. shareholders of a CFC also are required to include currently in income for U.S. tax purposes their pro rata shares of the corporation's untaxed earnings invested in certain items of U.S. property. This U.S. property generally includes tangible property located in the United States, stock of a U.S. corporation, an obligation of a U.S. person, and certain intangible assets, such as patents and copyrights, acquired or developed by the CFC for use in the United States. There are specific exceptions to the general definition of U.S. property, including for bank deposits, certain export property, and certain trade or business obligations. The inclusion rule for investment of earnings in U.S. property is intended to prevent taxpayers from avoiding U.S. tax on dividend repatriations by repatriating CFC earnings through non-dividend payments, such as loans to U.S. persons. **Subpart F Income** Under the subpart F rules, the United States generally taxes the 10-percent U.S. shareholders of a CFC on their pro rata shares of certain (generally passive) income of the CFC, without regard to whether the income is distributed to the	**I. TREATMENT OF DEFERRED FOREIGN INCOME UPON TRANSITION TO PARTICIPATION EXEMPTION SYSTEM OF TAXATION AND DEEMED REPATRIATION AT TWO-TIER RATE** **A. Overview.** New Section 965 generally requires that, for the last taxable year of a foreign corporation beginning before January 1, 2018, any U.S. shareholder of a deferred foreign income corporation must include in income their pro rata shares of the accumulated post-1986 deferred foreign income that was not previously taxed. A portion of that pro rata share of deferred foreign income is deductible; the amount deductible varies depending upon whether the deferred foreign income is held in the form of liquid or illiquid assets. The deduction results in a reduced rate of tax with respect to income from the required inclusion of pre-effective date earnings. A corresponding portion of the credit for foreign taxes is disallowed, thus limiting the credit to the taxable portion of the included income. The separate foreign tax credit limitation rules of present law section 904 apply, with coordinating rules. The increased tax liability generally may be paid over an eight-year period. Special rules are provided for S corporations and real estate investment trusts ("REITs"). **B. Subpart F inclusion of deferred foreign income.** The mechanism for the mandatory inclusion of pre-effective date foreign earnings is subpart F. Section 965(a) provides that the subpart F income of all specified foreign corporations is increased for the last taxable year that begins before January 1, 2018, by the greater of the accumulated post-1986 deferred	The provision applies to distributions made (and for purposes of determining a taxpayer's foreign tax credit limitation under section 904, deductions in taxable years beginning) after December 31, 2017.	§ 78 § 904 § 907 § 965

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shareholders. Subpart F income consists of foreign base company income (generally passive income such as dividends, interest, rents, and royalties) and a number of categories of income from business operations, including foreign base company sales income, foreign base company services income, and foreign base company oil-related income, and certain foreign insurance company income. U.S. shareholders of a CFC also are required to include currently in income for U.S. tax purposes their pro rata shares of the corporation's untaxed earnings invested in certain items of U.S. property. **<u>Subpart F Exceptions</u>** Several exceptions to the broad definition of subpart F income permit continued deferral for income from certain transactions, dividends, interest and certain rents and royalties received by a CFC from a related corporation organized and operating in the same foreign country in which the CFC is organized. 1. (Active Business Income?) 2. The same-country exception is not available to the extent that the payments reduce the subpart F income of the payor. 3. Any item of income received by a CFC if the taxpayer establishes that the income was subject to an effective foreign income tax rate greater than 90 percent of the maximum U.S. corporate income tax rate (that is, more than 90 percent of 35 percent, or 31.5 percent). 4. A provision colloquially referred to as the "CFC look-through" rule excludes from foreign personal holding company income dividends,	foreign income as of November 2, 2017, or December 31, 2017.[1] The amount so determined is includible in gross income under section 951 (hereinafter, "the section 951 inclusion").[2] The House Report provides that foreign corporations no longer in existence and for which there is no taxable year beginning or ending in 2017 are not within the scope of this provision.[3] Consistent with the general operation of subpart F, each U.S. shareholder of a specified foreign corporation must include in income its pro rata share of the foreign corporation's subpart F income attributable to its Section 951 inclusion. House Report; Senate Report. In contrast to the participation exemption deduction available only to domestic corporations that are U.S. shareholders under subpart F, the transition rule applies to all U.S. shareholders of a specified foreign corporation. **C. Application of New Section 965.** New Section 965 applies to all U.S. shareholders of a deferred foreign income corporation.[4] **1. Definition of Deferred Foreign Income Corporation.** Section 965(a) applies to a deferred foreign corporation. A deferred foreign income corporation means, with respect to any United States shareholder, any specified foreign corporation of such United States shareholder which has accumulated post-1986 deferred foreign income (as of the applicable dates of November 2, 2017, or December 31, 2017)) greater than zero.[5] **2. Definition of Specified Foreign Corporation.** A specified foreign corporation is		§ 78 § 904 § 907 § 965

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interest, rents, and royalties received or accrued by one CFC from a related CFC (with relation based on control) to the extent attributable or properly allocable to non-subpart-F income of the payor. 5. Previously taxed earnings and profits There is also an exclusion from subpart F income for certain income of a CFC that is derived in the active conduct of banking or financing business ("active financing income"), which applies to all taxable years of the foreign corporation beginning after December 31, 2014, and for taxable years of the shareholders that end during or within such taxable years of the corporation. With respect to income derived in the active conduct of a banking, financing, or similar business, a CFC is required to be predominantly engaged in such business and to conduct substantial activity with respect to such business in order to qualify for the active financing exceptions. In addition, certain nexus requirements apply, which provide that income derived by a CFC or a qualified business unit ("QBU") of a CFC from transactions with customers is eligible for the exceptions if, among other things, substantially all of the activities in connection with such transactions are conducted directly by the CFC or QBU in its home country, and such income is treated as earned by the CFC or QBU in its home country for purposes of such country's tax laws. Moreover, the exceptions apply to income derived from certain cross border transactions, provided that certain requirements are met. In the case of a securities dealer, an exception from foreign personal holding company income applies to any interest or dividend (or certain equivalent amounts) from any transaction, including	a. Any CFC;[6] and b. Any foreign corporation in which a domestic corporation is a U.S. shareholder[7] other than a PFIC that is not a CFC.[8] **3. Accumulated post-1986 deferred foreign income.** Accumulated post-1986 deferred foreign income of a specified foreign corporation that is the subject of the mandatory inclusion under Section 965(a) is the greater of the accumulated post-1986 deferred foreign income determined as of November 2, 2017 (the date of introduction of the bill) or as of December 31, 2017.[9] The term accumulated post-1986 deferred foreign income is all post-1986 earnings and profits except to the extent that such earnings are: a. Attributable to income that is effectively connected with the conduct of a trade or business in the United States and thus subject to current U.S. income tax,[10] or b. in the case of a CFC, if distributed, would be excludible from the gross income of a U.S. shareholder as previously taxed income under section 959.[11] **4. Post-1986 Earnings** and Profits. Post-1986 earnings and profits are those earnings that accumulated in taxable years beginning after 1986, computed in in accordance with sections 964(a) and 986, taking into account only periods when the foreign corporation was a specified foreign corporation.[12] Post-1986 foreign earnings and profits are not reduced by distributions during the taxable year to which	The provision applies to distributions made (and for purposes of determining a taxpayer's foreign tax credit limitation under section 904, deductions in taxable years beginning) after December 31, 2017.[124]	§ 78 § 904 § 907 § 965

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a hedging transaction or a transaction consisting of a deposit of collateral or margin, entered into in the ordinary course of the dealer's trade or business as a dealer in securities within the meaning of section 475.1434. In the case of a QBU of the dealer, the income is required to be attributable to activities of the QBU in the country of incorporation, or to a QBU in the country in which the QBU both maintains its principal office and conducts substantial business activity. A coordination rule provides that, for securities dealers, this exception generally takes precedence over the exception for active financing income. Income is treated as active financing income only if, among other requirements, it is derived by a CFC or by a QBU of that CFC. Certain activities conducted by persons related to the CFC or its QBU are treated as conducted directly by the CFC or QBU. An activity qualifies under this rule if the activity is performed by employees of the related person and if the related person is an eligible CFC, the home country of which is the same as the home country of the related CFC or QBU; the activity is performed in the home country of the related person; and the related person receives arm's-length compensation that is treated as earned in the home country. Income from an activity qualifying under this rule is excluded from subpart F income so long as the other active financing requirements are satisfied. Certain income of a qualifying branch of a qualifying insurance company with respect to risks located within the home country of the branch or within the CFC's country of creation or organization are also excepted from foreign personal holding company income, provided that certain requirements are met. Further, additional exceptions from	section 965 applies other than by dividends distributed to another specified foreign corporation.[13] **a. Reduction in Amounts Included in Gross Income of U.S. Shareholders of Specified Foreign Corporations with Deficits in Earnings and Profits.** The income inclusion required of a U.S. shareholder under Section 965 is reduced by the portion of aggregate foreign earnings and profits deficit allocated to that person by reason of that person's interest in an "E&P deficit foreign corporation."[14] An E&P deficit foreign corporation is defined as any specified foreign corporation with respect to which the taxpayer is a U.S. shareholder, if as of November 2, 2017: (1) such specified foreign corporation has a deficit in post-1986 earnings and profits;[15] (2) such corporation was a specified foreign corporation;[16] and (3) such taxpayer was a U.S. shareholder of such corporation.[17] The U.S. shareholder aggregates its pro rata share in the foreign E&P deficits of each such company and allocates such aggregate amount among the deferred foreign income corporations in which the shareholder is a U.S. shareholder.[18] The U.S. shareholder's aggregate E&P deficit is then allocated among the deferred foreign income corporations in the same ratio as the U.S. shareholder's pro rata share of post-1986 deferred foreign income in that corporation[19] bears to the U.S. shareholder's pro rata share of accumulated post-1986 deferred foreign income from all deferred foreign income corporations with respect to which the shareholder is a U.S. shareholder.[20] For the portion of aggregate E&P		§ 78 § 904 § 907 § 965

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insurance income and from foreign personal holding company income apply for certain income of certain CFCs or branches with respect to risks located in a country other than the United States, provided that the requirements for these exceptions, including reserve requirements, are met. **<u>Exclusion of previously taxed earnings and profits</u>** A 10-percent U.S. shareholder of a CFC may exclude from its income actual distributions of earnings and profits from the CFC that were previously included in the 10-percent U.S. shareholder's income under subpart F. Any income inclusion (under section 956) resulting from investments in U.S. property may also be excluded from the 10-percent U.S. shareholder's income when such earnings are ultimately distributed. Ordering rules provide that distributions from a CFC are treated as coming first out of earnings and profits of the CFC that have been previously taxed under subpart F, then out of other earnings and profits. **<u>Basis adjustments</u>** In general, a 10-percent U.S. shareholder of a CFC receives a basis increase with respect to its stock in the CFC equal to the amount of the CFC's earnings that are included in the 10-percent U.S. shareholder's income under subpart F. Similarly, a 10-percent U.S. shareholder of a CFC generally reduces its basis in the CFC's stock in an amount equal to any distributions that the 10-percent U.S. shareholder receives from the CFC that are excluded from its income as previously taxed under subpart F.	deficits that include qualified deficits, the portion of the deficit that is attributable to a qualified deficit, and the qualified activity, must be identified.[21] **b. Netting Among U.S. Shareholders in Same Affiliated Groups.** Section 965 also permits intragroup netting among U.S. shareholders in an affiliated group in which there is at least one U.S. shareholder with a net E&P surplus and another with a net E&P deficit.[22] The net E&P surplus shareholder may reduce its net surplus by the shareholder's applicable share of aggregate unused E&P deficit, based on the group's ownership percentage of the members.[23] For example, a U.S. corporation may have two domestic subsidiaries, X and Y, in which it owns 100 percent and 80 percent, respectively. If X has a $1,000 net E&P surplus, and Y has $1,000 net E&P deficit, X is an E&P net surplus shareholder, and Y is an E&P net deficit shareholder. The net E&P surplus of X may be reduced by the net E&P deficit of Y to the extent of the group's ownership percentage in Y, which is 80-percent. The remaining net E&P deficit of Y is unused. If the U.S. shareholder Z is also a wholly owned domestic subsidiary of the same U.S. parent as X and Y, the group ownership percentage of Y is unchanged, and the surpluses of X and Z are reduced ratably by 800 of the net E&P deficit of Y. **c. Treatment of Earnings and Profits in Future Years.** **(1) Reduced Earnings and Profits Treated as Previously Taxed Income When Distributed.** In taxable years beginning after 2017, amounts by which the section 951	The provision relating to transfer of loss amounts from foreign branches to certain foreign corporations is effective for transfers after December 31, 2017.	§ 78 § 904 § 907 § 965

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	inclusion was reduced by aggregate E&P deficits are considered as amounts included in the gross income of the U.S. shareholder.[24] **(2) Increase in Earnings and Profits for E&P Deficits.** The shareholder's pro rata share of the E&P of an E&P deficit foreign corporation that used qualified deficits to reduce its section 951 inclusion is increased by the amount of such deficit and attributed to the same activity to which the income was attributed.[25] **d. Reduced Earnings and Profits Treated as Previously Taxed Income When Distributed.** In taxable years beginning with the year of the section 951 inclusion under Section 965, amounts by which the section 951 inclusion was reduced by aggregate E&P deficits are considered as amounts included in the gross income of the U.S. shareholder for purposes of applying section 959.[26] **e. Example.** For example, assume that a foreign corporation organized after December 31, 1986 has $100 of accumulated earnings and profits as of November 2, 2017, and December 31, 2017 (determined without diminution by reason of dividends distributed during the taxable year and after any increase for qualified deficits), which consist of $120 general limitation earnings and profits and a $20 passive limitation deficit, the foreign corporation's post-1986 earnings and profits would be $100, even if the $20 passive limitation deficit was a hovering deficit. Foreign income taxes related to the hovering deficit, however, would not generally be deemed paid by the U.S. shareholder recognizing an incremental income inclusion. However, the	The provision is effective for sales or exchanges after December 31, 2017.	§ 78 § 904 § 907 § 965

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	conferees expect the Secretary may issue guidance to provide that, solely for purposes of calculating the amount of foreign income taxes deemed paid by the U.S. shareholder with respect to an inclusion under section 965, a hovering deficit may be absorbed by current year earnings and profits and the foreign income taxes related to the hovering deficit may be added to the specified foreign corporation's post-1986 foreign income taxes in that separate category on a pro rata basis in the year of inclusion.[27] **f. Guidance.** In order to avoid double-counting and double non-counting of earnings, the Conference Report provides that Treasury may provide guidance to adjust the amount of post-1986 earnings and profits of a specified foreign corporation to ensure that a single item of a specified foreign corporation is taken into account only once in determining the income of a United States shareholder subject to this provision. Such an adjustment may be necessary, for example, when there is a deductible payment (e.g., interest or royalties) from one specified foreign corporation to another specified foreign corporation between measurement dates.[28] **D. Participation exemption applied to accumulated post-1986 deferred foreign income.** A U.S. shareholder of a specified foreign corporation is allowed a deduction of a portion of the increased subpart F income attributable to the inclusion of pre-effective date deferred foreign income.[29] The amount of the deduction is the sum of the 15.5-percent rate equivalent percentage of the inclusion amount that is the shareholder's aggregate cash position		§ 78 § 904 § 907 § 965

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	and the 8-percent rate equivalent percentage of the portion of the inclusion that exceeds the aggregate cash position. By stating the permitted deduction in the form of a tax rate equivalent percentage, the provision ensures that all pre-effective date accumulated post-1986 deferred foreign income is subject to either a 8-percent or 15.5-percent rate of tax, depending on the underlying assets as of the measurement date, without regard to the corporate tax rate that may be in effect at the time of the inclusion. For example, corporate taxpayers that use a fiscal year as the taxable year may report the increased subpart F income in a taxable year for which a reduced corporate tax rate would otherwise apply, but the allowable deduction would be reduced such that the rate of U.S. tax on the income inclusion would be 8 or 15.5 percent.[31] **1. 8-Percent Rate Equivalent Percentage.** The term "8 percent rate equivalent percentage" means, with respect to any United States shareholder for any taxable year, the percentage which would result in the amount to which such percentage applies being subject to a 8 percent rate of tax determined by only taking into account a deduction equal to such percentage of such amount and the highest rate of tax applicable to corporations for such taxable year.[32] In the case of any taxable year of a United States shareholder to which section 15 applies, the highest rate of tax applicable to corporations before the effective date of the change in rates and the highest rate of tax applicable to corporations after the effective date of such change shall each be taken into account under the preceding sentence in the same		§ 78 § 904 § 907 § 965

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	Proportions as the portion of such taxable year which is before and after such effective date, respectively.[33] The calculation is based on the highest rate of tax applicable to corporations in the taxable year of inclusion, even if the U.S. shareholder is an individual. The Conf. Report provides that the use of rate equivalent percentages is intended to ensure that the rates of tax imposed on the deferred foreign income is similar for all U.S. shareholders, regardless of the year in which section 965 gives rise to an income inclusion. Individual U.S. shareholders, and the investors in U.S. shareholders that are pass-through entities generally can elect application of corporate rates for the year of inclusion. **2. 15.5-Percent Rate Equivalent.** The term "15.5 percent rate equivalent percentage" means, with respect to any United States shareholder for any taxable year, the percentage determined above for the 8-Percent rate equivalent percentage, but applied by substituting "15.5 percent rate of tax" for "8 percent rate of tax".[34] **E. Aggregate Cash Position.** The aggregate earnings and profits attributable to cash assets for a U.S. shareholder is the greater of the pro rata share of the cash position of all specified foreign corporations as of the last day of the last taxable year beginning before January 1, 2018, or the average of the cash position determined on the last day of each of the two taxable years ending immediately before November 2, 2017.[35] For purposes of this computation, the cash position of certain non-corporate entities that would be treated as specified foreign corporations if they were foreign	The provisions relating to sales or exchanges of stock apply to sales or exchanges after December 31, 2017. The provision relating to reduction of basis in certain foreign stock for the purposes of determining a loss is effective for distributions made after December 31, 2017. The provisions relating to transfer of loss amounts from foreign branches to certain foreign corporations and to the repeal of the active trade or business are effective for transfers after December 31, 2017.	§ 78 § 904 § 907 § 965

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	corporations is also included.[36] The Conference Report clarifies that the cash position of a U.S. shareholder does not generally include the cash attributable to a direct ownership interest in a partnership, but preserves the rule that cash positions of certain noncorporate foreign entities owned by a specified foreign corporation are taken into account if such entities would be specified foreign corporations with respect to the U.S. shareholder if the entity were a foreign corporation.[37] For example, if a U.S. shareholder owns a five-percent interest in a partnership, the balance of which is held by a specified foreign corporation with respect to which such shareholder is a U.S. shareholder, the partnership is treated as a specified foreign corporation with respect to the U.S. shareholder, and the cash or cash equivalents held by the partnership are includible in the aggregate cash position of the U.S. shareholder on a look-through basis. The conferees anticipate that the Secretary will provide guidance for taking into account only the specified foreign corporation's share of the partnership's cash position, and not the five-percent interest directly owned by the U.S. shareholder. The cash position of an entity consists of all cash, net accounts receivables, and the fair market value of similarly liquid assets, specifically including personal property that is actively traded on an established financial market (other than stock in the specified foreign corporation), government securities, certificates of deposit, commercial paper, and short-term obligations.[38] To avoid double counting of cash assets, a U.S. shareholder may disregard accounts receivable and short-term obligations of a specified foreign corporation if that shareholder		§ 78 § 904 § 907 § 965

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	can establish that the amounts were already taken into account by that shareholder with respect to another specified foreign corporation.39 Treasury is granted authority to identify other assets that are economically equivalent to the enumerated assets that are treated as cash.[40] The provision also authorizes Treasury to disregard transactions that are determined to have the principal purpose of reducing the aggregate foreign cash position.[41] **F. Special Rules.** In addition, the increase in income that is not taxed by reason of the partial deduction allowed under this provision is treated as income exempt from tax for purposes of determining the basis in an interest in a partnership or subchapter S corporation,[42] but not as income exempt from tax for purposes of determining the accumulated adjustments account of a subchapter S corporation.[43] Similarly, the Conference Report provides that the conferees expect the Secretary to provide regulations or other guidance that provide for similar treatment under section 986(c), such that any gain or loss recognized thereunder with respect to distributions of earnings previously taxed (or treated as previously taxed) by reason of section 965(a) will be diminished proportionately to the diminution of the net taxable income resulting from section 965(a) by reason of the deduction allowed under section 965(c). **G. Regulatory authority.** Section 965(o) grants Treasury regulatory authority to carry out the provisions of the section, including regulations or other guidance to provide appropriate basis adjustments. As another example, the Senate		§ 78 § 904 § 907 § 965

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	Report states that Treasury may identify instances in which it is appropriate to grant relief from potential double-counting of earnings and profits, which may occur due to different measurement dates applicable to specified foreign corporations within an affiliated group, or the timing of intragroup distributions. Section 965(o)(2) also specifies that Treasury shall prescribe rules or guidance in order to deter tax avoidance through use of entity classification elections and accounting method changes, among other possible strategies. The Conference Report states that "[t]he conferees are also aware that certain taxpayers may have engaged in tax strategies designed to reduce the amount of post-1986 earnings and profits in order to decrease the amount of the inclusion required under this provision. Such tax strategies may include a change in entity classification, accounting method, and taxable year, or intragroup transactions such as distributions or liquidations. The conferees expect the Secretary to prescribe rules to adjust the amount of post-1986 earnings and profits in such cases in order to prevent the avoidance of the purposes of this section."[44] The Conference Report further provides that the conferees expect that the Secretary will exercise his authority under the consolidated return provisions to appropriately limit the netting across chains of ownership within a group of related parties in the application of this provision. However, nothing in this provision is intended to be interpreted as limiting the Secretary's authority to use such regulatory authority to prescribe regulations on proper application of this section on		§ 78 § 904 § 907 § 965

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	a consolidated basis for affiliated groups filing a consolidated return.[45] **H. Foreign tax credits Reduced.** **1. No Credit or Deduction Allowed with Respect to a Certain Portion of Foreign Taxes.** A portion of foreign income taxes deemed paid or accrued with respect to the increased subpart F income attributable to the inclusion of pre-effective date deferred foreign income is not creditable against the Federal income tax attributable to the inclusion,[46] nor is it deductible.[47] The disallowed portion of foreign tax credits is calculated in Section 965(g)(2). The provision coordinates the disallowance of foreign tax credits with the requirement that a domestic corporate shareholder is deemed to receive a dividend in an amount equal to foreign taxes it is deemed to have paid and for which it claimed a credit.[48] Under the coordination rule, the foreign taxes treated as paid or accrued by a domestic corporation as a result of the inclusion are limited to the those taxes in proportion to the taxable portion of the section 965 inclusion. The gross-up amount equals the total foreign income taxes multiplied by the fraction, numerator of which is taxable portion of the increased subpart F income under this provision and the denominator of which is the total increase in subpart F income under this provision.[49] **2. Basis Adjustments.** The Conference Report States that basis adjustments (increases or decreases) may be necessary with respect to both the stock of the deferred foreign income corporation and the E&P deficit foreign corporation and authorizes the Secretary to provide for such basis adjustments or other		§ 78 § 904 § 907 § 965

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	adjustments, as may be appropriate. For example, with respect to the stock of the deferred foreign income corporation, Treasury may determine that a basis increase is appropriate in the taxable year of the section 951A inclusion or, alternatively, Treasury may modify the application of section 961(b)(1) with respect to such stock. Moreover, with respect to the stock of the E&P deficit corporation, Treasury may require a reduction in basis for the taxable year in which the U.S. shareholder's pro rata share of the earnings of the E&P deficit corporation are increased. **I. Installment payments.** A U.S. shareholder may elect to pay the net tax liability resulting from the mandatory inclusion of pre-effective-date undistributed CFC earnings in eight installments.[50] If installment payment is elected, the payments for each of the first five years equal 8 percent of the net tax liability, the sixth installment equals 15 percent of the net tax liability, increasing to 20 percent for the seventh installment and the remaining balance of 25 percent in the eighth year.[51] The net tax liability that may be paid in installments is the excess of the U.S. shareholder's net income tax for the taxable year in which the pre-effective-date undistributed CFC earnings are included in income over the taxpayer's net income tax for that year determined without regard to the inclusion and without regard to any income or deduction properly attributable to a dividend received by such U.S. shareholder from any deferred foreign income corporation.[52] An election to pay tax in installments must be made by the due date for the tax return for the taxable year in which the pre-effective-date undistributed CFC earnings are		§ 78 § 904 § 907 § 965

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	included in income. The Treasury Secretary has authority to prescribe the manner of making the election.[53] **1. Date for Payment of Installments.** The first installment must be paid on the due date (determined without regard to extensions) for the tax return for the taxable year of the income inclusion.[54] Succeeding installments must be paid annually no later than the due dates (without extensions) for the income tax return of each succeeding year.[55] **2. Proration of Deficiency of Installments.** If a deficiency is later determined with respect to the net tax liability, the additional tax due generally may be prorated among all installment payments.[56] The portions of the deficiency prorated to an installment that was due before the deficiency was assessed must be paid upon notice and demand.[57] The portion prorated to any remaining installment is payable with the timely payment of that installment payment, unless the deficiency is attributable to negligence, intentional disregard of rules or regulations, or fraud with intent to evade tax, in which case the entire deficiency is payable upon notice and demand.[58] **3. Interest.** The timely payment of an installment does not incur interest. If a deficiency is determined that is attributable to an understatement of the net tax liability due under this provision, the deficiency is payable with underpayment interest for the period beginning on the date on which the net tax liability would have been due, without regard to an election to pay in installments, and ending with the payment of the deficiency. Furthermore, any amount of		§ 78 § 904 § 907 § 965

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	deficiency prorated to a remaining installment also bears interest on the deficiency, but not on the original installment amount.[59] **4. Acceleration of Payment.** The provision also includes an acceleration rule. If (1) there is a failure to pay timely any required installment, (2) there is a liquidation or sale of substantially all of the U.S. shareholder's assets (including in a bankruptcy case), (3) the U.S. shareholder ceases business, or (4) another similar circumstance arises, the unpaid portion of all remaining installments is due on the date of the event (or, in a title 11 case or similar proceeding, the day before the petition is filed).[60] This rule does not apply to the sale of substantially all the assets of a taxpayer to a buyer if such buyer enters into an agreement with Treasury under which such buyer is liable for the remaining installments due under this subsection in the same manner as if such buyer were the taxpayer.[61] **J. Limitations on assessment extended.** Section 965(k) provides an exception to the otherwise applicable limitations period for assessment of tax to ensure that the period for assessment of underpayments in tax related to the treatment of the pre-effective date foreign earnings does not expire prior to six years from the date on which the return initially reflecting the section 951 inclusion was filed.[62] **K. Special rule for S corporations.** **1. General Rule.** A special rule permits deferral of the transition net tax liability for shareholders of a U.S. shareholder that is an S corporation.[63] The S corporation is required to report on its income tax return the amount		§ 78 § 904 § 907 § 965

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	includible in gross income by reason of this provision, as well as the amount of deduction thatwould be allowable, and provide a copy of such information to its shareholders.[64] Any shareholder of the S corporation may elect to defer his portion of the net tax liability at transition to the participation exemption system until the shareholder's taxable year in which a triggering event occurs.[65] The election to defer the tax is due not later than the due date for the return of the S corporation for its last taxable year that begins before January 1, 2018.[66] **2. Triggering Events.** Three types of events may trigger an end to deferral of the net tax liability: a. The corporation ceases to be an S corporation (determined as of the first day of the first tax year that such corporation is not an S corporation);[67] b. A liquidation or sale of substantially all corporate assets (including in a bankruptcy or similar case), a cessation of business by such S corporation, such S corporation ceases to exist, or any similar circumstance;[68] and c. A transfer of shares of stock in the S corporation by the electing taxpayer (including by reason of death, or otherwise),[69] unless the transferee of the stock agrees with the Secretary to be liable for net tax liability in the same manner as the transferor.[70] Partial transfers trigger the end of deferral only with respect to the portion of tax properly allocable to the portion of stock sold.[71]		§ 78 § 904 § 907 § 965

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	3. Joint and Several Liability of S Corporation. If a shareholder of an S corporation has elected deferral under the special rule for S corporation shareholders and a triggering event occurs, the S corporation and the electing shareholder are jointly and severally liable for any net tax liability and related interest or penalties.[72] **4. Extension of Limitation on Assessment.** The period within which the IRS may collect such liability does not begin before the date of an event that triggers the end of the deferral.[73] **5. Annual Reporting of Net Tax Liability.** If an election to defer payment of the net tax liability is in effect for a shareholder, that shareholder must report the amount of the deferred net tax liability on each income tax return due during the period that the election is in effect.[74] Failure to include that information with each income tax return will result in a penalty equal to five-percent of the amount that should have been reported.[75] **6. Election to Pay Deferred Liability in Installments.** **a. Eligibility for Election.** After a triggering event occurs, a shareholder is the S corporation may elect to pay the net tax liability in eight installments in accordance with the rules governing installment payments.[76] Whether a shareholder may elect to pay in installments depends upon the type of event that triggered the end of deferral. If the triggering event is a liquidation, sale of substantially all corporate assets, cessation of business by such S corporation, such S corporation ceases to exist or		§ 78 § 904 § 907 § 965

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	similar circumstance, an installment payment election can be made only with the consent of the IRS.[77] **b. Timing of Election.** The installment election is due with the timely return for the year in which the triggering event occurs.[78] **c. Due Date of First Installment.** The first installment payment is required by the due date of the same return, determined without regard to extensions of time to file.[79] **L. Election Not to Apply Net Operating Loss Deduction.** A U.S. shareholder may elect, no later than with a timely filed return for the taxable year, not to take into account the Section 951 inclusion (or any related deemed paid foreign tax credits treated as dividends by reason of Section 78) (1) in determining the amount of its net operating loss deduction for such tax year; or (2) in determining the amount of taxable income for such tax year which may be reduced by NOL carryovers or carrybacks.[80] **M. Special rules for REITs.** To alleviate the burden of compliance with this section by REITs, special rules are provided if a U.S. shareholder is a REIT.[81] **N. Effective Date.** The provision is effective on date of enactment. Act Sec. 14103. **II. DEDUCTION FOR FOREIGN-SOURCE PORTION OF DIVIDENDS RECEIVED BY DOMESTIC CORPORATIONS FROM SPECIFIED 10-PERCENT OWNED FOREIGN CORPORATIONS** **A. In general.** New Section 245A generally establishes a participation exemption system for foreign income. This exemption is		§ 78 § 904 § 907 § 965

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	provided for by means of a 100-percent deduction for the foreign-source portion of dividends received from specified 10-percent owned foreign corporations by domestic corporations that are United States shareholders of those foreign corporations within the meaning of section 951(b) (referred to here as "participation DRD").[82] Specifically, Section 245A(a) provides that, "[i]n the case of any dividend received from a specified 10-percent owned foreign corporation by a domestic corporation which is a United States shareholder with respect to such foreign corporation, there is allowed as a deduction an amount equal to the foreign-source portion of such dividend." The Conference Report provides that the DRD is available only to C corporations that are not RICs or REITs.[83] **B. Definitions.** **1. Specified Foreign Corporation.** A specified 10-percent owned foreign corporation is any foreign corporation with respect to which any domestic corporation is a United States shareholder with respect to such corporation.[84] (Under section 951(b), a domestic corporation is a United States shareholder of a foreign corporation if it owns, within the meaning of section 958(a), or is considered as owning by applying the rules of section 958(b), 10 percent or more of the voting stock or value of the foreign corporation.) Such term does not include any corporation which is a passive foreign investment company with respect to the shareholder and which is not a controlled foreign corporation.[85]		§ 78 § 904 § 907 § 965

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	2. Dividends Received. The Conference Report states that the term "dividend received" is intended to be interpreted broadly, consistently with the meaning of the phrases "amount received as dividends" and "dividends received" under sections 243 and 245, respectively.[86] The House Report provides that consequently, for example, gain included in gross income as a dividend under section 1248(a) or 964(e) would constitute a dividend received for which the deduction under section 245A may be available.[87] The statute grants Treasury the authority to prescribe such regulations or other guidance as may be necessary or appropriate to carry out the provisions of section 245A. The House Report indicates that Congressional intent is that such regulations would clarify the intended broad scope of the term "dividend received."[88] The intended broad scope of dividends received is provided in the Conf. Report by the following example: For example, if a domestic corporation indirectly owns stock of a foreign corporation through a partnership and the domestic corporation would qualify for the participation DRD with respect to dividends from the foreign corporation if the domestic corporation owned such stock directly, the domestic corporation would be allowed a participation DRD with respect to its distributive share of the partnership's dividend from the foreign corporation.[89] **3. Foreign-source portion of a dividend.** The participation DRD is available only for the foreign-source portion of dividends received from a specified 10-percent owned foreign corporation.[90] The foreign-source portion of any dividend is the amount that bears		§ 78 § 904 § 907 § 965

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	the same ratio to the dividend as the undistributed foreign earnings of the 10-percent owned foreign corporation bears to the total undistributed earnings of the foreign corporation.[91] Undistributed earnings are the amount of the earnings and profits of a specified 10-percent owned foreign corporation (Computed in accordance with secs. 964(a) and 986) as of the close of the taxable year of the specified 10-percent owned foreign corporation in which the dividend is distributed and not reduced by dividends[92] distributed during that taxable year.[93] Undistributed foreign earnings are the portion of the undistributed earnings attributable to neither income described in section 245(a)(5)(A) nor section 245(a)(5)(B), without regard to section 245(a)(12).[94] **C. Foreign tax credit disallowance; foreign tax credit limitation** **1. Foreign Tax Credit Disallowance.** No foreign tax credit[95] or deduction[96] is allowed for any taxes (including withholding taxes) paid or accrued with respect to a dividend that qualifies for the participation DRD. **2. Foreign Tax Credit Limitation Amount.** For purposes of computing the section 904(a) foreign tax credit limitation, a domestic corporation that is a U.S. shareholder of a specified 10-percent owned foreign corporation must compute its foreign-source taxable income (and entire taxable income) by disregarding the foreign-source portion of any dividend received from that foreign corporation for which the DRD is taken, and any deductions properly allocable or apportioned to income (other than amounts includible under section 951(a)(1) or 951A(a))		§ 78 § 904 § 907 § 965

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	with respect to stock of such specified 10-percent owned foreign corporation, or (ii) such stock to the extent income with respect to such stock is other than amounts includible under section 951(a)(1) or 951A(a).[97] **D. Hybrid Dividends.** The DRD is not allowed for any dividend received by a U.S. shareholder from a controlled foreign corporation if the dividend is a hybrid dividend.[98] A hybrid dividend is an amount received from a controlled foreign corporation for which a deduction would be allowed under this provision and for which the specified 10-percent owned foreign corporation received a deduction (or other tax benefit) with respect to from taxes imposed by a foreign country or possession of the United States.[99] If a controlled foreign corporation with respect to which a domestic corporation is a U.S. shareholder receives a hybrid dividend from any other controlled foreign corporation with respect to which the domestic corporation is also a U.S. shareholder, then the hybrid dividend is treated for purposes of section 951(a)(1)(A) as subpart F income of the recipient controlled foreign corporation (notwithstanding section 954(c)(6)) for the taxable year of the controlled foreign corporation in which the dividends was received and the U.S. shareholder includes in gross income an amount equal to the shareholder's pro rata share of the subpart F income, determined in the same manner as section 951(a)(2).[100] The rules denying a foreign tax credit apply to any hybrid dividend received by, or any amount included under paragraph (2) in the gross income of, a United States shareholder.[101]		§ 78 § 904 § 907 § 965

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	E. Holding period requirement. A domestic corporation is not permitted a DRD in respect of any dividend on any share of stock that is held by the domestic corporation for 365 days or less during the 731-day period beginning on the date that is 365 days before the date on which the share becomes ex-dividend with respect to the dividend.[102] For this purpose, the holding period requirement is treated as met only if the specified 10-percent owned foreign corporation is a specified 10-percent owned foreign corporation at all times during the period[103] and the taxpayer is a U.S. shareholder with respect to such specified 10-percent owned foreign corporation at all times during the period.[104] **F. Special Rule for Purging Distributions of Passive Foreign Investment Companies.** Any amount which is treated as a dividend under section 1291(d)(2)(B) shall not be treated as a dividend for purposes of this section.[105] **G. Special rules relating to sales or transfers involving specified 10-percent owned foreign corporations** **1. Sales by United States persons of stock.** In the case of the sale or exchange by a domestic corporation of stock in a foreign corporation held for one year or more, any amount received by the domestic corporation which is treated as a dividend for purposes of section 1248, is treated as a dividend for purposes of applying the provision.[106] This amendment applies to sales or exchanges after December 31, 2017.[107]		§ 78 § 904 § 907 § 965

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	2. Reduction in basis of certain foreign stock. Solely for the purpose of determining a loss, a domestic corporate shareholder's adjusted basis in the stock of a specified 10-percent owned foreign corporation is reduced by an amount equal to the portion of any dividend received with respect to such stock from such foreign corporation that was not taxed by reason of a dividends received deduction allowable under section 245A in any taxable year of such domestic corporation. This rule applies in coordination with section 1059 (providing for reduction of corporate shareholder's basis in stock by nontaxed portion of extraordinary dividends), such that any reduction in basis required pursuant to this provision will be disregarded, to the extent the basis in the specified 10-percent owned foreign corporation's stock has already been reduced pursuant to section 1059.[108] This amendment is effective for distributions made after December 31, 2017.[109] **3. Inclusion of transferred loss amount in certain assets transfers.** **a. General Rule.** If a domestic corporation transfers substantially all of the assets of a foreign branch (within the meaning of section 367(a)(3)(C) as in effect before enactment of the Act) to a foreign corporation which, after such transfer, is a specified 10-percent owned foreign corporation with respect to which the domestic corporation is a United States shareholder, the domestic corporation is required to include in gross income an amount equal to the transferred loss amount, subject to certain limitations.[110]		§ 78 § 904 § 907 § 965

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	b. Transferred Loss Amount. The transferred loss amount is the excess of: (1) losses incurred by the foreign branch after December 31, 2017[111] for which a deduction was allowed to the domestic corporation,[112] over (2) the sum of (a) taxable income earned by the foreign branch for a taxable year after the taxable year in which the loss was incurred and through the close of the taxable year of the transfer[113] and (b) gain recognized by reason of an overall foreign loss recapture arising out of disposition of assets on account of the underlying transfer.[114] **c. Reduction for Recognized Gains.** The transferred loss amount is reduced by the amount of gain recognized by the taxpayer (other than gain recognized by reason of an overall foreign loss recapture) on account of the transfer.[115] Under a transition rule in the Act, the amount of gain taken into account under this provision is reduced by the amount of gain which would be recognized under section 367(a)(3)(C) (determined without regard to the amendments made by subsection (e)) with respect to losses incurred before January 1, 2018. [116] **d. Source of Income.** Amounts included in gross income by reason of the provision are treated as derived from sources within the United States.[117] **e. Basis of Adjustments.** Consistent with regulations or guidance that Treasury may prescribe, proper adjustments are made in the adjusted basis of the taxpayer's stock in the specified 10-percent owned foreign corporation to which the transfer is made, and in the transferee's adjusted basis in the property transferred, to reflect amounts included in gross income under this provision.[118]		§ 78 § 904 § 907 § 965

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	4. Sale by a CFC of a lower-tier CFC. **a. General Rule.** If for any taxable year of a CFC beginning after December 31, 2017, an amount is treated as a dividend under section 964(e)(1) because of a sale or exchange by the CFC of stock in another foreign corporation held for one year or more, then: (i) the foreign-source portion of the dividend is treated as subpart F income of the selling CFC for purposes of section 951(a)(1)(A),[119] (ii) a United States shareholder with respect to the selling CFC includes in gross income for the taxable year of the shareholder with or within the taxable year of the CFC ends, an amount equal to the shareholder's pro rata share (determined in the same manner as under section 951(a)(2)) of the amount treated as subpart F income under (i),[120] and (iii) the deduction under section 245A(a) is allowable to the United States shareholder with respect to the subpart F income included in gross income under (ii) in the same manner as if the subpart F income were a dividend received by the shareholder from the selling CFC.[121] **b. Foreign-Source Portion.** The foreign-source portion of any amount treated as a dividend under this provision is determined in the same manner as under Section 245A(c).[122] **c. Application of Basis or Similar Adjustment.** In the case of a sale or exchange by a CFC of stock in another corporation in a taxable year of the selling CFC beginning after December 31, 2017, to which this provision applies if gain were recognized, rules similar to section 961(d) apply.[123]		§ 78 § 904 § 907 § 965

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	III. REPEAL OF ACTIVE TRADE OR BUSINESS EXCEPTION **A. Repeal of Active Trade or Business Exception.** Section 367 is amended to provide that in connection with any exchange described in section 332, 351, 354, 356, or 361, if a U.S. person transfers property used in the active conduct of a trade or business to a foreign corporation, such foreign corporation shall not, for purposes of determining the extent to which gain shall be recognized on such transfer, be considered to be a corporation. [1] I.R.C. § 965(a). [2] Senate Report [3] House Report. [4] I.R.C. § 965(a); I.R.C. § 965(d)(1). [5] I.R.C. § 965(d)(1). [6] I.R.C. § 965(e)(1)(A). [7] I.R.C. § 965(e)(1)(B). [8] I.R.C. § 965(e)(3). [9] I.R.C. § 965(a). [10] I.R.C. § 965(d)(2)(A). [11] I.R.C. § 965(d)(2)(B). [12] I.R.C. § 965(d)(3). [13] I.R.C. § 965(d)(3)(B). [14] I.R.C. § 965(b)(1). [15] I.R.C. § 965(b)(3)(B)(i). [16] I.R.C. § 965(b)(3)(B)(ii). [17] I.R.C. § 965(b)(3)(B)(iii). [18] I.R.C. § 965(b)(2). [19] I.R.C. § 965(b)(2)(A). [20] I.R.C. § 965(b)(2)(B). [21] I.R.C. § 965(b)(3)(A)(ii). [22] I.R.C. § 965(b)(5)(A).		§ 78 § 904 § 907 § 965

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	[23] I.R.C. § 965(b)(5). [24] I.R.C. § 965(b)(4)(A). [25] I.R.C. § 965(b)(4)(B). [26] I.R.C. § 965(b)(4)(A). [27] *Cf.* Treas. Reg. sec. 1.367(b)-7(d)(2)(ii) and (iii). [28] Conf. Report. [29] I.R.C. § 965(c)(1). [30] I.R.C. § 965(c)(1). [31] House Report. [32] I.R.C. § 865(c)(2)(A). [33] I.R.C. § 865(c)(2)(A). [34] I.R.C. § 965(c)(2)(B). [35] I.R.C. § 965(c)(3)(A). [36] I.R.C. § 965(c)(3)(E). [37] Conf. Report. [38] I.R.C. § 965(c)(3)(B)(iii). [39] I.R.C. § 965(c)(3)(D). [40] I.R.C. § 965(c)(3)(B)(iii)(V). [41] I.R.C. § 965(c)(3)(F). [42] I.R.C. § 965(f)(2)(A). [43] I.R.C. § 965(f)(2)(B). [44] Conf. Report. [45] Conf. Report. [46] I.R.C. § 965(g)(1). [47] I.R.C. § 965(g)(2). [48] I.R.C. § 965(g)(4). [49] I.R.C. § 965(g)(4). [50] I.R.C. § 965(h)(1). [51] I.R.C. § 965(h)(1). [52] I.R.C. § 965(h)(6). [53] I.R.C. § 965(h)(5) [54] I.R.C. § 965(h)(2). [55] I.R.C. § 965(h)(2).		§ 78 § 904 § 907 § 965

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	[56] I.R.C. § 965(h)(4). [57] I.R.C. § 965(h)(4). [58] I.R.C. § 965(h)(4). [59] Senate Report. [60] I.R.C. § 965(h)(3). [61] I.R.C. 965(h)(3). [62] I.R.C. § 965(k). [63] I.R.C. § 965(i)(1). [64] I.R.C. § 965(j). [65] I.R.C. § 965(i)(1). [66] I.R.C. § 965(i)(8). [67] I.R.C. § 965(i)(2)(A)(i). [68] I.R.C. § 965(i)(2)(A)(ii). [69] I.R.C. § 965(i)(2)(A)(iii). [70] I.R.C. § 965(i)(2)(C). [71] I.R.C. § 965(i)(2)(B). [72] I.R.C. § 965(i)(5). [73] I.R.C. § 965(i)(6). [74] I.R.C. § 965(i)(7)(A). [75] I.R.C. § 965(i)(7)(C). [76] I.R.C. § 965(i)(4)(A). [77] I.R.C. § 965(i)(4)(D). [78] I.R.C. § 965(i)(4)(B). [79] I.R.C. § 965(i)(4)(C). [80] I.R.C. § 965(n)(1) [81] *See* I.R.C. § 965(m). [82] I.R.C. § 245A(a). [83] Conf. Report. [84] I.R.C. § 245A(b)(1) [85] I.R.C. § 245A(b)(2) [86] Conf. Report. [87] House Report. [88] House Report. [89] Conf. Report. [90] *See* I.R.C. § 245A(a).		§ 78 § 904 § 907 § 965

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	III. Global Intangible Low-Taxed Income (“GILTI”) **1. Overview** Under new section 951A, each U.S. shareholder of any CFC must include in gross income for a taxable year its global intangible low-taxed income (“GILTI”) in a manner generally similar to inclusions of subpart F income. GILTI means, with respect to any U.S. shareholder for the shareholder’s taxable year, the excess (if any) of the shareholder’s net CFC tested income over the shareholder’s net deemed tangible income return. Thus, the GILTI calculation can be expressed as follows: *GILTI – Net CFC Tested Income – Net Deemed Tangible Income Return* The new law effectively provides domestic corporations with reduced rates of U.S. tax on GILTI. In the case of domestic corporations for taxable years beginning after December 31, 2017, and before January 1, 2026, the new law generally allows as a deduction an amount equal to the sum of 50 percent of its GILTI (if any). For taxable years beginning after December 31, 2025, the deduction for GILTI is lowered to 37.5 percent. Thus, the effective U.S. tax rate on GILTI (with respect to domestic corporations) is 10.5 percent for taxable years beginning after December 31, 2017, and before January 1, 2026. For domestic corporations in taxable years beginning after December 31, 2025, the effective U.S. tax rate on GILTI is 13.125 percent. **2. Net CFC Tested Income** Net CFC tested income is defined, with respect to any U.S. shareholder, as the excess of		

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	the aggregate of the shareholder's pro rata share of the tested income of each CFC with respect to which it is a U.S. shareholder over the aggregate of its pro rata share of the tested loss of each CFC with respect to which it is a U.S. shareholder. Pro rata shares are determined under the rules of section 951(a)(2). The formula for net CFC tested income can be expressed as follows: *Net CFC Tested Income = Sum of CFC Tested Income – Sum of CFC Tested Loss* The tested income of a CFC means the excess (if any) of the gross income of the corporation—determined without regard to certain exceptions to tested income—over deductions (including taxes) properly allocable to such gross income (referred to in this document as "tested gross income"). The exceptions to tested income are: (1) the corporation's ECI under section 952(b); (2) any gross income taken into account in determining the corporation's subpart F income; (3) any gross income excluded from foreign base company income or insurance income by reason of the high-tax exception under section 954(b)(4); (4) any dividend received from a related person (as defined in section 954(d)(3)); and (5) any foreign oil and gas extraction income (as defined in section 907(c)(1)). The tested loss of a CFC means the excess (if any) of deductions (including taxes) properly allocable to the corporation's gross income—determined without regard to the tested income exceptions—over the amount of such gross income.		

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	3. Net Deemed Tangible Income Return The shareholder's net deemed tangible income return is, with respect to any U.S. shareholder for a taxable year, the excess (if any) of 10 percent of the aggregate of its pro rata share of the QBAI of each CFC with respect to which it is a U.S. shareholder over the amount of interest expense taken into account in determining its net CFC tested income for the taxable year to the extent that the interest expense exceeds the interest income properly allocable to the interest expense that is taken into account in determining its net CFC tested income. As a result, the formula for GILTI is effectively as follows: *GILTI = Net CFC Tested Income – [10% * QBAI) – Interest Expense]* **4. Qualified Business Asset Investment** QBAI is defined, with respect to any CFC for a taxable year, as the average of the aggregate of its adjusted bases, determined as of the close of each quarter of the taxable year, in specified tangible property used in its trade or business and of a type with respect to which a deduction is generally allowable under section 167. For these purposes, the adjusted basis in any property must be determined using the alternative depreciation system under current section 168(g). Specified tangible property means any property used in the production of tested income. If such property was used in the production of both tested income and income that is not tested income (i.e., dual-use property), the property is treated as specified tangible property in the same proportion that the amount of tested gross income		

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	produced with respect to the property bears to the total amount of gross income produced with respect to the property. For purposes of determining a CFC's QBAI and its adjusted basis in specified tangible property, the adjusted basis is determined by allocating the depreciation deduction with respect to the property ratably to each day during the period in the taxable year to which the depreciation relates. In addition, if a CFC holds an interest in a partnership at the close of the CFC's taxable year, the CFC takes into account its distributive share of the aggregate of the partnership's adjusted bases (determined as of such date in the hands of the partnership) in tangible property held by the partnership to the extent that the property is used in the trade or business of the partnership, is of a type with respect to which a deduction is allowable under section 167, and is used in the production of tested income (determined with respect to the CFC's distributive share of income with respect to the property). The CFC's distributive share of the adjusted basis of any property is the CFC's distributive share of income with respect to the property. The Treasury is specifically authorized to issue anti-avoidance regulations or other guidance as appropriate, including regulations or other guidance that provide for the treatment of property if the property is transferred or held temporarily, or if avoidance was a factor in the transfer or holding of the property.		

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	5. Coordination with Subpart F Although GILTI inclusions do not constitute subpart F income, GILTI inclusions are generally treated similarly to subpart F inclusions. Thus they are generally treated in the same manner as amounts included under section 951(a)(1)(A) for purposes of applying sections 168(h)(2)(B), 535(b)(10), 904(h)(1), 959, 961, 962, 993(a)(1)(E), 996(f)(1), 1248(b)(1), 1248(d)(1), 6501(e)(1)(C), 6654(d)(2)(D), and 6655(e)(4). However, the Secretary may provide rules for coordinating the GILTI inclusion with provisions of law in which the determination of subpart F income is required to be made at the CFC level. The provision requires that the amount of GILTI included by a U.S. shareholder be allocated across each CFC with respect to which it is a U.S. shareholder. The portion of GILTI treated as being with respect to a CFC equals zero for a CFC with no tested income and, for a CFC with tested income, the portion of GILTI which bears the same ratio to the total amount of GILTI as the U.S. shareholder's pro rata amount of tested income of the CFC bears to the aggregate amount of the U.S. shareholder's pro rata amount of the tested income of each CFC with respect to which it is a U.S. shareholder. For a CFC with tested income, the following formula expresses how to determine the portion of GILTI treated as being with respect to the CFC: *CFC's GILTI = GILTI x (Share of CFC's Tested Income / Share of Agg. CFC Tested Income)* For purposes of the GILTI inclusion, a person is treated as a U.S. shareholder of a CFC		

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	for any taxable year only if such person owns (within the meaning of section 958(a)) stock in the corporation on the last day, in such year, on which the corporation is a CFC. A corporation is generally treated as a CFC for any taxable year if the corporation is a CFC at any time during the taxable year. **6. Deemed-Paid Credit for Taxes Properly Attributable to Tested Income** For any amount of GILTI included in the gross income of a domestic corporation, the corporation's deemed-paid credit equals 80 percent of the product of the corporation's inclusion percentage multiplied by the aggregate tested foreign income taxes paid or accrued, with respect to tested income, by each CFC with respect to which the domestic corporation is a U.S. shareholder. The inclusion percentage is defined, with respect to any domestic corporation, as the ratio (expressed as a percentage) of such corporation's GILTI amount divided by the aggregate amount of its pro rata share of the tested income of each CFC with respect to which it is a U.S. shareholder (referred to as "aggregate tested income"). Tested foreign income taxes is defined, with respect to any domestic corporation that is a U.S. shareholder of a CFC, as the foreign income taxes paid or accrued by the CFC that are properly attributable to the CFC's tested income. The deemed-paid credit with respect to the GILTI inclusion can be expressed in the following formula:		

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	*Deemed-Paid Credit = 80% * (GILTI / Aggregate Tested Income) * Aggregate Tested Foreign Income Tax* The new law creates a separate foreign tax credit basket for GILTI, with no carryforward or carryback available for excess credits. For purposes of determining the foreign tax credit limitation, GILTI is not general category income, and income that is both GILTI and passive category income is considered passive category income. The taxes deemed to have been paid are treated as an increase in GILTI for purposes of section 78, determined by taking into account 100 percent of the product of the inclusion percentage and aggregate tested foreign income taxes (instead of 80 percent in the determination of the deemed-paid credit). Therefore, the section 78 gross-up can be expressed in the following formula: *Section 78 Gross-Up = 100% * (GILTI / Aggregate Tested Income) * Aggregate Tested Foreign Income Tax* **IV. Foreign-Derived Intangible Income (“FDII”)** New section 250 effectively provides domestic corporations with reduced rates of U.S. tax on their foreign-derived intangible income (“FDII”). The FDII of any domestic corporation is determined on a formulaic basis as the amount that bears the same ratio to the corporation’s deemed intangible income as its foreign-derived deduction eligible income bears to its deduction eligible income. In other words, a domestic corporation’s FDII is its deemed intangible income multiplied by the percentage of its deduction eligible income that is foreign derived.		

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	The calculation can also be expressed as the following: *FDII = Deemed Intangible Income x (Foreign Derived Deduction Eligible Income / Deduction Eligible Income)* In the case of domestic corporations for taxable years beginning after December 31, 2017, and before January 1, 2026, the new law generally allows as a deduction an amount equal to 37.5 percent of its FDII. For taxable years beginning after December 31, 2025, the deduction for FDII is reduced to 21.875 percent. **1. Deduction Eligible Income** Deduction eligible income is defined, with respect to any domestic corporation, as the excess (if any) of the gross income of the corporation—determined without regard to certain exceptions to deduction eligible income—over deductions (including taxes) properly allocable to such gross income (referred to as “deduction eligible gross income”). The exceptions to deduction eligible income are: (1) the subpart F income of the corporation determined under section 951; (2) the GILTI of the corporation; (3) any financial services income (as defined in section 904(d)(2)(D)) of the corporation; (4) any dividend received from a CFC with respect to which the corporation is a U.S. shareholder; and (5) any domestic oil and gas extraction income of the corporation; and (6) any foreign branch income (as defined in section 904(d)(2)(J)) of the corporation. The formula for deduction eligible income can generally be expressed as follows: *Deduction Eligible Income = Gross Income – Exceptions – Allocable Deductions*		

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	2. Deemed Intangible Income The domestic corporation's deemed intangible income is defined as the excess (if any) of its deduction eligible income over its deemed tangible income return. The deemed tangible income return is defined, with respect to any corporation, as an amount equal to 10 percent of the corporation's qualified business asset investment ("QBAI"). Deemed intangible income can be calculated as follows: *Deemed Intangible Income – Deduction Eligible Income – (10% x QBAI)* For purposes of computing its FDII, a domestic corporation's QBAI is the average of the aggregate of its adjusted bases, determined as of the close of each quarter of the taxable year, in specified tangible property used in its trade or business and of a type with respect to which a deduction is allowable under section 167. The adjusted basis in any property must be determined using the alternative depreciation system under section 168(g), notwithstanding any provision of law. Specified tangible property is defined as any tangible property used in the production of deduction eligible income. If such property was used in the production of deduction eligible income and income that is not deduction eligible income (i.e., dual-use property), the property is treated as specified tangible property in the same proportion that the amount of deduction eligible gross income produced with respect to the property bears to the total amount of gross income produced with respect to the property. In other words, the percentage of a domestic		

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	corporation's adjusted basis in dual-use property that is included in QBAI equals the deduction eligible gross income produced with respect to the property divided by the total gross income produced with respect to the property. **3. Foreign-Derived Deduction Eligible Income** Foreign-derived deduction eligible income is defined, with respect to a taxpayer for its taxable year, as any deduction eligible income of the taxpayer that is derived in connection with (1) property that is sold by the taxpayer to any person who is not a United States person and that the taxpayer establishes to the satisfaction of the Secretary is for a foreign use or (2) services provided by the taxpayer that the taxpayer establishes to the satisfaction of the Secretary are provided to any person, or with respect to property, not located within the United States. Foreign use means any use, consumption, or disposition that is not within the United States. Special rules for determining foreign use apply to transactions that involve property or services provided to domestic intermediaries or related parties. For these purposes, the terms "sold," "sells", and "sale" include any lease, license, exchange, or other disposition. **(a) Property or Services Provided to Domestic Intermediaries** If a taxpayer sells property to another person (other than a related party) for further manufacture or modification within the United States, the property is generally not treated as sold for a foreign use even if such other person subsequently uses such property for foreign use.		

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	However, there is an exception to this general rule for property (1) that is ultimately sold by a related party, or used by a related party in connection with property that is sold or the provision of services, to another person who is an unrelated party who is not a U.S. person and (2) that the taxpayer establishes to the satisfaction of the Secretary is for a foreign use. Deduction eligible income derived in connection with services provided to another person (other than a related party) located within the United States is not treated as foreign-derived deduction eligible income, even if the other person uses the services in providing services the income from which is considered foreign-derived deduction eligible income. **(b) Special Rules with Respect to Related Party Transactions** If property is sold to a related foreign party, the sale is not treated as for a foreign use unless the property is sold by the related foreign party to another person who is unrelated and is not a U.S. person and the taxpayer establishes to the satisfaction of the Secretary that such property is for a foreign use. Income derived in connection with services provided to a related party who is not located in the United States is not treated as foreign-derived deduction eligible income unless the taxpayer establishes to the satisfaction of the Secretary that such service is not substantially similar to services provided by the related party to persons located within the United States. For purposes of applying these rules, a related party means any member of an affiliated group as defined in section 1504(a) determined		

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	by substituting "more than 50 percent" for "at least 80 percent" each place it appears and without regard to sections 1504(b)(2) and 1504(b)(3). Any person (other than a corporation) is treated as a member of the affiliated group if the person is controlled by members of the group (including any entity treated as a member of the group by reason of this sentence) or controls any member, with control being determined under the rules of section 954(d)(3). **V. The Base Erosion Minimum Tax Amount ("BEAT")** Under new section 59, an applicable taxpayer is required to pay a tax equal to the base erosion minimum tax amount for the taxable year. The base erosion minimum tax amount is the excess of 10 percent (5 percent for one year for base erosion payments paid or accrued in tax years beginning after December 31, 2017) of the modified taxable income of the taxpayer for the taxable year over an amount equal to the regular tax liability (defined in section 26(b)) of the taxpayer for the taxable year reduced (but not below zero) by the excess (if any) of the credits allowed under Chapter 1 against such regular tax liability over the sum of: (1) the credit allowed under section 38 for the taxable year which is properly allocable to the research credit determined under section 41(a), plus (2) the portion of the applicable section 38 credits not in excess of 80 percent of the lesser of the amount of such credits or the base erosion minimum tax amount (determined without regard to this clause (2)). For taxable years beginning after December 31, 2025, two changes apply: (A) the 10-percent		

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	provided for above is changed to 12.5-percent, and (B) the regular tax liability is reduced by the aggregate amount of the credits allowed under Chapter 1 (and no other adjustment is made). Applicable section 38 credits means the credit allowed under section 38 for the taxable year which is properly allocable to: (A) the low-income housing credit determined under section 42(a), (B) the renewable electricity production credit determined under section 45(a), and (C) the investment credit determined under section 46, but only to the extent properly allocable to the energy credit determined under section 48. To determine its modified taxable income, the applicable taxpayer computes its taxable income for the year without regard to any base erosion tax benefit with respect to any base erosion payment or the base erosion percentage of any allowable net operating loss deduction allowed under section 172 for the taxable year. **1. Applicable Taxpayers and Related Parties** Applicable taxpayer is defined, with respect to any taxable year, as a taxpayer: (A) which is a corporation other than a regulated investment company, a real estate investment trust, or an S corporation; (B) the average annual gross receipts of the corporation for the three-taxable-year period ending with the preceding taxable year are at least $500 million, and (C) the base erosion percentage (as defined above) of the corporation for the taxable year is three percent or higher.		

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	In the case of a foreign person the gross receipts of which are taken into account for purposes of this provision, only gross receipts which are taken into account in determining income effectively connected with the conduct of a trade or business within the United States is taken into account. If a foreign person's gross receipts are aggregated with a U.S. person's gross receipts for reasons described in the aggregation rules below, the preceding sentence does not apply to the gross receipts of any U.S. person which are aggregated with the taxpayer's gross receipts. All persons treated as a single employer under section 52(a) are treated as one person for purposes of this provision, except that in applying section 1563 for purposes of section 52, the exception for foreign corporations under section 1563(b)(2)(C) is disregarded (called the "aggregation rules"). In addition, for purposes of this provision, foreign person has the meaning given in section 6038A(c)(3). **2. Base Erosion Payments** A base erosion payment means any amount paid or accrued by a taxpayer to a foreign person that is a related party of the taxpayer and with respect to which a deduction is allowable under Chapter 1. Such payments include any amount paid or accrued by the taxpayer to the related party in connection with the acquisition by the taxpayer from the related party of property of a character subject to the allowance of depreciation (or amortization in lieu of depreciation). A base erosion payment includes any premium or other consideration paid or accrued by the taxpayer to		

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	a foreign person which is a related party of the taxpayer for any reinsurance payments taken into account under sections 803(a)(1)(B) or 832(b)(4)(A). Base erosion payments do not include any amount that constitutes reductions in gross receipts including payments for costs of goods sold. However, base erosion payment includes any amount that constitutes reductions in gross receipts of the taxpayer that is paid or accrued by the taxpayer with respect to: (1) a surrogate foreign corporation which is a related party of the taxpayer, but only if such person first became a surrogate foreign corporation after November 9, 2017, or (2) a foreign person that is a member of the same expanded affiliated group as the surrogate foreign corporation. A surrogate foreign corporation has the meaning given in section 7874(a)(2), but does not include a foreign corporation treated as a domestic corporation under section 7874(b). **(a) Services Cost Method** A base erosion payment does not include any amount paid or accrued by a taxpayer for services if such services meet the requirements for eligibility for use of the services cost method described in Treas. Reg. sec. 1.482-9, as in effect as of the date of enactment of TCJA, without regard to the requirement that the services not contribute significantly to fundamental risks of business success or failure and only if the payments are made for services that have no markup component.		

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Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	(i) Qualified Derivative Payments Any qualified derivative payment is not treated as a base erosion payment. A qualified derivative payment means any payment made by a taxpayer pursuant to a derivative with respect to which the taxpayer: (i) recognizes gain or loss as if such derivative were sold for its fair market value on the last business day of the taxable year (and such additional times as are required by this title or the taxpayer's method of accounting), (ii) treats any gain or loss so recognized as ordinary, and (iii) treats the character of all items of income, deduction, gain or loss with respect to a payment pursuant to the derivative as ordinary. No payment is treated as a qualified derivative payment unless the taxpayer includes in the information required to be reported under section 6038B(b)(2) with respect to such taxable year such information as is necessary to identify the payments to be so treated and such other information as the Secretary of the Treasury determines necessary to carry out the provision. The rule for qualified derivative payments does not apply if a payment with respect to a derivative is in substance, or is disguising, the kind of payment that would be treated as a base erosion payment if it were not made pursuant to a derivative, including any interest, royalty, or service payment, (or any other payment subject to this provision) or in the case of a contract which has derivative and nonderivative components, the payment is properly allocable to the nonderivative component.		

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	For these purposes, the term derivative means any contract (including any option, forward contract, futures contract, short position, swap, or similar contract) the value of which, or any payment or other transfer with respect to which, is (directly or indirectly) determined by reference to one or more of the following: (i) any share of stock of a corporation, (ii) any evidence of indebtedness, (iii) any commodity which is actively traded, (iv) any currency, (v) any rate, price, amount, index, formula, or algorithm. Except as otherwise provided by the Secretary of the Treasury, American depository receipts and similar instruments with respect to shares of stock in foreign corporations are treated as shares of stock in such foreign corporations. The term derivative does not include any item described in paragraphs (i) through (v) above nor shall the term 'derivative' include any insurance, annuity, or endowment contract issued by an insurance company to which subchapter L applies (or issued by any foreign corporation to which such subchapter would apply if such foreign corporation were a domestic corporation). **(ii) Base Erosion Tax Benefit** A base erosion tax benefit means: (i) any deduction allowed under Chapter 1 for the taxable year with respect to a base erosion payment, (ii) in the case of a base erosion payment with respect to the purchase of property of a character subject to the allowance for depreciation (or amortization in lieu of depreciation), any deduction allowed in Chapter 1 for depreciation or amortization in lieu of depreciation with respect to the property acquired with such payment, or (iii) any reduction in gross		

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	receipts with respect to a payment described above with respect to a surrogate foreign corporation (as defined there) in computing gross income of the taxpayer for the taxable year. Any base erosion tax benefit attributable to any base erosion payment on which tax is imposed by sections 871 or 881 and with respect to which tax has been deducted and withheld under sections 1441 or 1442, is not taken into account in computing modified taxable income as defined above. The amount not taken into account in computing modified taxable income is reduced under rules similar to the rules under section 163(j)(5)(B). **(iii) Base Erosion Percentage** The base erosion percentage means for any taxable year, the percentage determined by dividing the aggregate amount of base erosion tax benefits of the taxpayer for the taxable year by the aggregate amount of the deductions allowable to the taxpayer under Chapter 1 for the taxable year, taking into account base erosion tax benefits described above and by not taking into account any deduction allowed under sections 172, 245A or 250 for the taxable year, any deduction for amounts paid or accrued for services to which the exception for the services cost method (as described above) applies, and any deduction for qualified derivative payments which are not treated as a base erosion payment as described above. **3. Information Reporting Requirements** The new law authorizes the Treasury to prescribe additional reporting requirements under section 6038A relating to: (A) the name, principal place of		

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Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
	business, and country or countries in which organized or resident of each person which: (i) is a related party to the reporting corporation, and (ii) had any transaction with the reporting corporation during its taxable year, (B) the manner of relation between the reporting corporation and the person referred to in (A), and (C) transactions between the reporting corporation and each related foreign person. In addition, for purposes of information reporting under sections 6038A and 6038C, if the reporting corporation or the foreign corporation to which section 6038C applies is an applicable taxpayer, the information that may be required includes: (A) base erosion payments paid or accrued during the taxable year by the taxpayer to a foreign person which is a related party of the taxpayer, (B) such information as the Secretary of the Treasury finds necessary to determine the base erosion minimum amount of the taxpayer for the taxable year, and (C) such other information as the Secretary of the Treasury determines is necessary. The penalties provided for under sections 6038A(D)(1) and (2) are both increased to $25,000.		

INTERNATIONAL TAX PROVISIONS – OTHER

Pre-Reform Law	Tax Cuts & Jobs Act	Effective Date	I.R.C. Sections
A U.S. shareholder of a CFC is subject to U.S. tax under subpart F on foreign base company oil related income regardless of whether the CFC distributes such income to the U.S. Shareholder.	**Repeal of treatment of foreign base company oil related income as subpart F income** The Act repeals foreign base company oil related income as subpart F income under §954. Stock attribution rules for determining CFC status are modified to treat a U.S. corporation as constructively owning stock held by its foreign shareholder.	The provision is effective for taxable years of foreign corporations beginning after December 31, 2017, and for taxable years of U.S. shareholders in which or with which such taxable years of foreign corporations end.	§ 954(a)
A provision colloquially referred to as the "CFC look-through" rule excludes from foreign personal holding company income dividends, interest, rents, and royalties received or accrued by one CFC from a related CFC (with relation based on control) to the extent attributable or properly allocable to non-subpart-F income of the payor.	**Look-thru rule for related controlled foreign corporations made permanent.** The provision makes the exclusion from foreign personal holding company income for certain dividends, interest (including factoring income that is treated as equivalent to interest under section 954(c)(1)(E)), rents, and royalties received or accrued by one CFC from a related CFC permanent.	The proposal is effective for taxable years of foreign corporations beginning after December 31, 2017, and for taxable years of U.S. shareholders in which or with which such taxable years of foreign corporations end.	§ 954(c)(6)
Section 951(b) defines a U.S. shareholder as a U.S. person who owns, or is considered as owning by applying the rules of ownership of §958(b), 10% or more of the total combined voting power of all classes of stock entitled to vote of such foreign corporation. Section 958(b)(4) prevents the attribution of stock ownership from a foreign person to a U.S. person. Section 951(a)(1) requires that foreign corporation be a controlled foreign corporation (CFC) for an uninterrupted period of 30 days or more before it is classified as a CFC for tax purposes.	**Modification of stock attribution rules for determining CFC status** The conference agreement follows the Senate amendment. In adopting this provision, the conferees intend to render ineffective certain transactions that are used to as a means of avoiding the subpart F provisions. One such transaction involves effectuating "de-control" of a foreign subsidiary, by taking advantage of the section 958(b)(4) rule that effectively turns off the constructive stock ownership rules of 318(a)(3) when to do otherwise would result in a U.S. person being treated as owning stock owned by a foreign person. Such a transaction converts former CFCs to non-CFCs, despite continuous ownership by U.S. shareholders.	The provision is effective for the last taxable year of foreign corporations beginning before January 1, 2018 and each subsequent year of such foreign corporations and for the taxable years of U.S. shareholders in which or with which such taxable years of foreign corporations end.	§ 318 § 958

MODIFICATIONS TO ESTATE, GIFT AND GENERATION SKIPPING TRANSFER TAXES: WHAT NOW?

- General Observations:
  - Further Decrease in Persons Subject to Estate/Gift Taxes.
  - Shift in Thinking of Estate Planning Professionals
  - Planning Alternatives: - It's Planning for a Reducing Exemption and Alternatives Based on Degree of Wealth - All Over Again
  - Planning with Flexibility to Address Sunsetting of Increase in Exemption
    - Nontaxable/taxable powers of appointment
    - Broad distribution powers in independent trustees
    - Use of trust protectors
    - QTIP planning
  - Review Current Plans, Especially Those with Formula Clauses
  - The estate tax exclusion amount has not increased for nonresident alien individuals with U.S. situs assets ($60K), so special planning needs continue for them

MODIFICATIONS TO ESTATE, GIFT AND GENERATION SKIPPING TRANSFER TAXES: WHAT NOW?

- Lifetime Gifts Between 1/1/18 and 12/31/25
  - Planning to avoid/minimize taxable gifts may not be necessary or appropriate
  - Opportunities for generation-skipping planning
  - Generation-skipping tax implications need to be considered (including late allocations of GST exemption)
  - Upstream gifts to secure basis adjustment at donee's death
  - Spousal Lifetime Access Trusts
  - Grantor Retained Annuity Trusts
  - Domestic Asset Protection Trusts
  - Transfers of Life Insurance
  - Forgiving outstanding loans to children
  - Gifts to IDGTs
  - Opportunity to equalize with respect to previous gifts to children/grandchildren
  - Audit cushion for gifts substantially less than the $11 million exemption
  - Ability to increase "seed funding" of IDGTs for sales to trusts
  - Clawback?

MODIFICATIONS TO ESTATE, GIFT AND GENERATION SKIPPING TRANSFER TAXES: WHAT NOW?

- Planning for Deathtime Disposition for Married Persons – General Guidelines
  - Spouses with Assets Under $5 Million (the unadjusted “sunset” amount) – Trust for Surviving Spouse vs. Outright/Basis Adjustment Considerations.
    - Make Clients Aware of Advantages/Flexibilities of Trusts
  - Spouses with Assets Between $5 million and $11 Million – Plan for possible need to utilize predeceasing spouse’s exemption with outright gift (disclaimer trust planning/QTIPable trust planning), taking into account portability election alternative.
  - Spouses with Assets Over $11 Million: Plan along same lines as spouses with assets between $5 million and $11 million, plus lifetime gifts to use the increased exemption amount.
  - Increase in Importance of Portability Election Analysis to Lock in Increased Unused Exemption of Predeceasing Spouse to Provide Surviving Spouse with Both Exemptions plus Full Basis Adjustment

TAX RATES

Taxable Income	Tax rate (percent)
Not over $50,000	15
Over $50,000 but not over $75,000	25
Over $75,000 but not over $10,000,000	34
Over $10,000,000	35

BONUS DEPRECIATION RATES

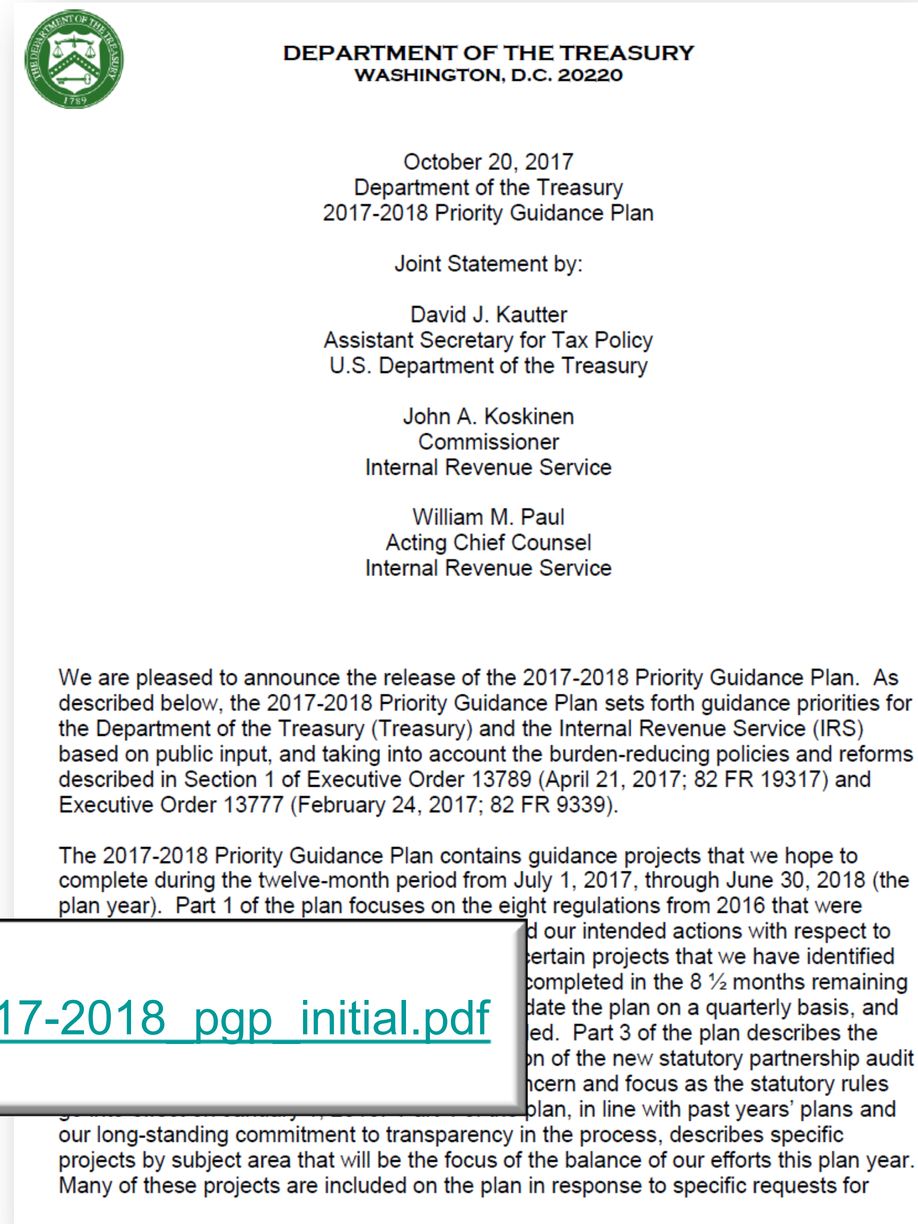
Placed in Service Year	Bonus Depreciation Percentage	
	Qualified Property in General	Qualified Property in General
2017	50 percent	50 percent
2018	40 percent	50 percent[1]
2019	30 percent	40 percent
2020	None	30 percent[2]

[1] It is intended that for longer production period property placed in service in 2018, 50 percent applies to the entire adjusted basis. Similarly, for longer production period property placed in service in 2019, 40 percent applies to the entire adjusted basis. A technical correction may be necessary with respect to longer production period property placed in service in 2018 and 2019 so that the statute reflects this intent.

[2]438 In the case of longer production period property described in section 168(k)(2)(B) and placed in service in 2020, 30 percent applies to the adjusted basis attributable to manufacture, construction, or production before January 1, 2020, and the remaining adjusted basis does not qualify for bonus depreciation. Thirty percent applies to the entire adjusted basis of certain aircraft described in section 168(k)(2)(C) and placed in service in 2020.

PHASE DOWN OF PORTION OF BASIS OF QUALIFIED PROPERTY

Placed in Service Year[6]	Phase Down of Portion of Basis of Qualified Property Acquired before Sept. 28, 2017	
	Qualified Property in General/Specified Plants	Longer Production Period Property and Certain Aircraft
Bonus Depreciation Percentage		
Sept. 28, 2017 – Dec. 31, 2017	50 percent[7]	50 percent[8]
2018	40 percent[9]	50 percent[10]
2019	30 percent[11]	40 percent[12]
2020	None[13]	30 percent[14]
2021 and thereafter	None[15]	None[16]
Portion of Basis of Qualified Property Acquired after Sept. 27, 2017		
Sept. 28, 2017 – Dec. 31, 2022	100 percent[17]	100 percent[18]
2023	80 percent[19]	100 percent[20]
2024	60 percent[21]	80 percent[22]
2025	40 percent[23]	60 percent[24]
2026	20 percent[25]	40 percent[26]
2027	None	20 percent[27]
2028 and thereafter	None	None



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

October 20, 2017
Department of the Treasury
2017-2018 Priority Guidance Plan

Joint Statement by:

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We are pleased to announce the release of the 2017-2018 Priority Guidance Plan. As described below, the 2017-2018 Priority Guidance Plan sets forth guidance priorities for the Department of the Treasury (Treasury) and the Internal Revenue Service (IRS) based on public input, and taking into account the burden-reducing policies and reforms described in Section 1 of Executive Order 13789 (April 21, 2017; 82 FR 19317) and Executive Order 13777 (February 24, 2017; 82 FR 9339).

The 2017-2018 Priority Guidance Plan contains guidance projects that we hope to complete during the twelve-month period from July 1, 2017, through June 30, 2018 (the plan year). Part 1 of the plan focuses on the eight regulations from 2016 that were
d our intended actions with respect to
ertain projects that we have identified
completed in the 8 ½ months remaining
date the plan on a quarterly basis, and
ed. Part 3 of the plan describes the
n of the new statutory partnership audit
ncern and focus as the statutory rules
plan, in line with past years' plans and
our long-standing commitment to transparency in the process, describes specific projects by subject area that will be the focus of the balance of our efforts this plan year. Many of these projects are included on the plan in response to specific requests for

https://www.irs.gov/pub/irs-utl/2017-2018_pgp_initial.pdf

2018 Standard Mileage Rates

Notice 2018-03

SECTION 1. PURPOSE

This notice provides the optional 2018 standard mileage rates for taxpayers to use in computing the deductible costs of operating an automobile for business, charitable, medical, or moving expense purposes. This notice also provides the amount taxpayers must use in calculating reductions to basis for depreciation taken under the business standard mileage rate, and the maximum standard automobile cost that may be used in computing the allowance under a fixed and variable rate (FAVR) plan.

SECTION 2. BACKGROUND

Rev. Proc. 2010-51, 2010-51 I.R.B. 883, provides rules for computing the deductible costs of operating an automobile for business, charitable, medical, or moving

r substantiating, under § 274(d) of the Internal Revenue Code

he Tax Regulations, the amount of ordinary and necessary

l transportation or travel away from home. Taxpayers using

the standard mileage rates must comply with Rev. Proc. 2010-51. However, a taxpayer is not required to use the substantiation methods described in Rev. Proc. 2010-51, but

https://www.irs.gov/pub/irs-drop/n-18-03.pdf

Guidance under Section 965

Notice 2018-07

SECTION 1. OVERVIEW

This notice announces that the Department of the Treasury ("Treasury Department") and the Internal Revenue Service ("IRS") intend to issue regulations for determining amounts included in gross income by a United States shareholder under section 951(a)(1) by reason of section 965 of the Internal Revenue Code ("Code") as amended by "An Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018," P.L. 115-97 (the "Act"), which was enacted on December 22, 2017. Section 2 of this notice provides background on section 965. Section 3 of this notice describes regulations that the Treasury Department and the IRS intend to issue. Section 4 of this notice describes the effective dates of those regulations. Section 5 of this notice requests comments and provides contact information.

SECTION 2. BACKGROUND

.01 Treatment of Accumulated Post-1986 Deferred Foreign Income as Subpart F Income

Section 965(a) provides that for the last taxable year of a deferred foreign income

efore January 1, 2018 (such year of the DFIC, the "inclusion

e corporation (as otherwise determined for such taxable year

sed by the greater of (1) the accumulated post-1986 deferred

foreign income of such corporation determined as of November 2, 2017, or (2) the accumulated post-1986 deferred foreign income of such corporation determined as of December 31, 2017

https://www.irs.gov/pub/irs-drop/n-18-07.pdf