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# 2017 New Tax Law: Overview of Provisions

*This client alert is part of a special series on the Tax Cuts and Jobs Act and related changes to the tax code, where Blank Rome's lawyers share their analysis of different provisions in the Act and how they may affect you and your business, along with specific action items. To see the full list of client alerts in this series, please click **here**.*

On December 20, 2017, Congress passed its comprehensive tax reform bill, the Tax Cuts and Jobs Act ("the Act" or "the Bill"), which is expected to be signed into law by President Trump in early January 2018. The Bill represents one of the most extensive modifications to the U.S. tax code in recent history, significantly modifying U.S. taxation for individuals and businesses. Most provisions in the bill take effect on January 1, 2018.

## TAX CUTS AND JOBS ACT—OVERVIEW OF PROVISIONS

Below please find a summary of just some of the provisions included in the Tax Cuts and Jobs Act, which have been identified under two categories—Individual Tax Reform and Corporate Tax Reform. Articles with additional information and action items by provision will also be circulated in the near future and as part of the "2017 New Tax Law" series.

## INDIVIDUAL TAX REFORM PROVISIONS

*The individual tax provisions in the bill, including the pass-through deduction, sunset after December 31, 2025.*

- **Modification of individual tax brackets.** There will be seven tax brackets for individuals (as opposed to six currently), with the top bracket's rate reduced from 39.6 percent to 37 percent.

- **Increase in standard deduction.** The standard deduction available to taxpayers who elect not to itemize deductions will be nearly doubled. The standard deduction for married individuals filing jointly will be increased from $12,000 to $24,000, and from $6,350 to $12,000 for single filers.

- **Repeal of limitation on itemized deductions.** Under current law, the total amount of most otherwise allowable itemized deductions is limited for certain high-income taxpayers. Beginning in 2018, this limitation on itemized deductions is repealed.

- **Personal exemptions repealed.** Personal exemptions currently allowed for certain taxpayers and their dependents will be eliminated. For 2017, the amount

deductible for each personal exemption is $4,050, but is phased out for joint filers with AGI in excess of $313,800 ($261,500 for single filers). The amount of tax required to be withheld from wages by employers is based in part on the number of withholding exemptions claimed on an employee's Form W-4. Beginning in 2018, personal exemptions are repealed, and the Secretary of the Treasury is to develop new rules for determining the amount of tax required to be withheld from wages.

- **Deduction for pass-through entities.** In a provision intended to benefit business activity conducted through flow-through entities, the Bill allows individuals (including trusts and estates) a deduction for 20 percent of the individual's "qualified business income" from flow-through entities, subject to a limitation based either on wages paid, or wages paid plus a capital element. Qualified businesses generally include any trade or business other than a "specified service business" such as a law firm, accounting firm, or other business whose primary activity is the provision of skilled services. However, the deduction may apply to service income attributable to a specified service trade or business where a taxpayer's taxable income is less than $315,000 (joint filers), or $157,000 (other filers), subject to a phase-out. Qualified items of income include 20 percent of any dividends from a real estate investment trust, as well as 20 percent of includable dividends from qualified publicly traded partnership income, but do not include certain service related income such as payments by a partnership to a partner in exchange for services.

- **Expansion of child tax credit.** The child tax credit is temporarily increased beginning in 2018 from $1,000 per qualifying child to $2,000 per qualifying child, and eligibility for the credit is expanded as the AGI threshold for phase out is increased from $110,000 to $400,000 for joint filers, and $75,000 to $200,000 for individual filers.

- **Limitations on losses.** Beginning in 2018, excess business losses for individual taxpayers are disallowed for the taxable year, but may be carried forward and treated as part of the taxpayer's net operating loss carryforward.

- **Modification of deduction for mortgage and home equity interest.** Beginning in 2018, the deduction for mortgage interest will be limited to acquisition indebtedness of up to $750,000. For taxpayers who entered into a contract to purchase a home prior to December 15, 2017, the limitation is increased to $1,000,000. The deduction currently allowable for interest on home equity indebtedness will be eliminated.

- **Modification of state and local tax deductions.** Generally, under the Bill, the deduction for state and local property taxes and state and local sales taxes is allowed only when paid or accrued in connection with a trade or business. For personal taxes not related to a trade or business, the deduction is limited to $10,000 for aggregate state and local property and income taxes.

- **Repeal of deduction for casualty and theft losses.** The deduction currently allowed for personal casualty and theft losses is repealed, except for losses attributable to certain disasters declared by the President.

- **Modification of charitable contribution deduction.** The Bill retains and expands the charitable contribution by increasing the percentage limit for charitable contributions of cash made to public charities.

- **Repeal of deduction for alimony payments.** Alimony and separate maintenance payments are currently deductible by the payor spouse and includible in income by the recipient spouse. For any divorce or separation instrument executed after December 31, 2018, alimony payments will not be deductible by the payor spouse, nor includible in income by the recipient.

- **Modification of alternative minimum tax.** The AMT exemption amounts are increased from $86,200 to $109,400 for joint filers and from $55,400 to $70,300 for single unmarried filers. Such exemption amounts are reduced (not below zero) to an amount equal to 25 percent of the amount by which AMT income exceeds $1 million for joint filers and $500,000 for all other filers, which represent increases from current threshold amounts.

- **Increase in estate and gift tax exemption.** The estate and gift tax exemption is doubled to $10 million (indexed for inflation) for estates and gifts made after December 31, 2017 and before January 1, 2026.

- **Carried interest.** Partnership interests received in connection with the performance of services, including carried interests must be held for three years before they can qualify for long-term capital gain treatment, effectively recharacterizing certain gains attributable to applicable partnership interests from long-term to short-term capital gain.

- **Affordable Care Act.** The individual mandate penalty will be repealed.

## BUSINESS TAX REFORM PROVISIONS

- **Corporate tax rate.** The corporate tax rate will be a flat 21 percent rate, as opposed to the current graduated rates, with the top rate currently at 35 percent.

- **Dividends received deduction ("DRD").** Under current law, a corporation is allowed a DRD of 80 percent of the related dividend from a 20 percent-owned domestic corporation, and a DRD of 70 percent of the related divided from other corporations. The 80 percent and 70 percent rates will be reduced to 65 percent and 50 percent, respectively.

- **Alternative minimum tax.** The corporate alternative minimum tax will be eliminated. The current corporate AMT rate is 20 percent, with an exemption amount of up to $40,000.

- **Section 179 property expensing.** The maximum amount of qualifying property that can be expensed under Section 179 in a given tax year will be increased to $1 million (from $500,000), and the phase-out threshold will be increased to $2.5 million (from $2 million).

- **Cost recovery of qualifying business assets.** The current 50 percent bonus depreciation is increased to 100 percent for qualified assets placed in service after September 27, 2017 and before December 31, 2022. For assets placed after 2022, the amount of bonus expensing allowed will decline by 20 percent each year until it phases out completely for qualified property placed in service after December 31, 2026.

- **Limitations on business interest deduction.** Taxpayers will be subject to a disallowance of a deduction for net interest expense in excess of 30 percent of the taxpayer's net adjusted taxable income, which is calculated before net operating losses, depreciation, amortization, and depletion. A special rule applies to pass-through entities, which requires the disallowance to be determined at the entity level (i.e., at the partnership level rather than the partner level). An exemption from this limitation applies for taxpayers with average annual gross receipts for a rolling three-year tax period that do not exceed $25 million.

- **Net operating loss.** Net operating losses arising after tax years beginning after December 31, 2017 will be carried forward indefinitely, as opposed to the current carryforward period of 20 years, but may only offset 80 percent of taxable income. Further, the current two-year carryback period will be repealed.

- **Like-kind exchanges.** Effective for transfers after December 31, 2017, the rule allowing the deferral of gain on like-kind exchanges is modified to allow for like-kind exchanges only with respect to real property that is not held primarily for sale. That is, deferral would no longer be allowed for exchanges of intangible property, or tangible personal property such as artwork.

- **Cash method of accounting.** Under current law, C corporations and partnerships with a C corporation partner may use the cash method of accounting only if its average annual gross receipts did not exceed $5 million during the three-year period ending with the previous tax year (the "gross receipts test"). For tax years beginning after December 31, 2017, the gross receipts test is modified such that a taxpayer may use the cash method of accounting if, during the three-year period ending with the previous tax year, its average annual gross receipts do not exceed $25 million.

- **Excessive employee compensation.** Under current law, a deduction for compensation paid to a "covered employee" of a publicly traded corporation is limited to $1 million per year, with exceptions for commissions and performance-based compensation. The Bill repeals these exceptions, and clarifies the definition of "covered employee" to include the principal executive officer, the principal financial officer, and the three other highest paid employees. Further, once an individual is a covered employee, he or she will remain a covered employee for all future tax years.

- **Movement to territorial tax system.** The Bill movies the U.S. closer to a territorial tax system by providing a 100 percent DRD for foreign-source dividends received by U.S. corporations from certain foreign subsidiaries, effective for distributions made after 2017. The 100 percent DRD would only be available to certain domestic C corporations that are neither real estate investment trusts nor regulated investment companies. Dividends from passive foreign investment companies also would not qualify for the 100 percent DRD.

- **One-time repatriation.** As part of the transition to a more territorial tax system, there will be a one-time repatriation tax on certain foreign subsidiaries' previously untaxed foreign earnings and profits ("E&P"). Generally, this "repatriation toll charge" will apply to post-1986 E&P of a controlled foreign corporation, or a foreign corporation that is at least 10 percent owned by a U.S. corporation. Foreign tax credits for the portion of earnings subject to the toll charge would be available to offset the tax.

- **Unrelated business Taxable income ("UBTI").** Tax-exempt organizations will be required to separately calculate the net UBTI of each unrelated trade or business. Losses derived from one unrelated trade or business may no longer offset income from another unrelated trade or business. Current law allows a tax-exempt organization, in calculating UBTI, which operates multiple unrelated trades or business to aggregate income and deductions from all such trades and business.

- **Excise tax on investment income of private colleges and universities.** For tax years beginning after December 31, 2017, an excise tax equal to 1.4 percent is imposed on net investment income of private university and colleges with at least 500 tuition-paying students (who are more than 50 percent located in the U.S.) and with assets, other than used for the institution's exempt purpose, of at least $500,000 per student. Currently, private universities and colleges are not subject to excise tax on net investment income.

**Clients who would like more information about their specific circumstances should contact a member of Blank Rome's Tax, Benefits, and Private Client practice group.**

**Authors of this client alert:**

**Lawrence S. Chane**
**215.569.5721 | chane@blankrome.com**

**Cory G. Jacobs**
**215.569.5481 | cjacobs@blankrome.com**