

# Tax Essentials For Small Business

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## ACPE # 0130-9999-19-160-L04-P&T

### Conflict of Interest: Contractual Relationship with American Pharmacies

#### LEARNING OBJECTIVES

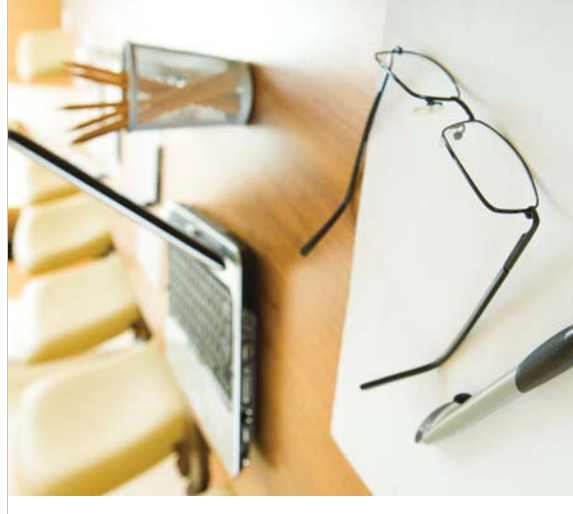
- Describe the main provisions of the 2017 Tax Cuts & Jobs Act;
- Explain relevant income tax changes that apply to retail pharmacy;
- Discuss important provisions of IRC Sec. 199A (Qualified Business Income Deduction);
- List changes to the deductibility of entertainment & meals expenses; and
- Identify key planning opportunities for individuals and businesses in future tax years.

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# Tax Cuts & Jobs Act – Business & Individual Provisions

## Many changes!

- Guidance is needed
- Effect on tax provisions
- Effect on financial statements
- Ease of filing (?)



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## 2018 EXAMINATION RATES

- Overall Exam Rate in 2018 = 0.5%. Down 7% from 2017.
- Individual Return Rates = 0.59%. (1 out of 178)
  - 81% correspondence exams
- Sole Proprietors with > \$250,000 Gross = 2.4%
- Individuals between \$200,000-\$1,000,000.00 = 0.6%
- Individuals > \$1,000,000.00 = 3.2%
- C Corps = 0.9%
- Partnerships & S Corps = 0.2%
- Special Exams for 403(b) Plans for improperly excluding eligible employees

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## Overview of Business Changes

- Corporate rate reduction to flat 21%
- Repeal of corporate AMT
- Special rules for pass-throughs (Sec. 199A)
  - Limit on use of and carryback of NOL, can now only carry forward and 80% limit
- Expensing of assets
  - increases to Sec.179 (\$1 million and threshold \$2.5 million)
- Expanded accounting method exceptions for small businesses
- Changes to various fringe benefits including treatment of meals and entertainment paid by employer
- Corporate shift from worldwide to territorial system

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## Corporate Rate Changes

- Flat rate of 21%, this might be a game changer
- Effective for years beginning after 12/31/17
- Personal service corporations taxed at same rate (no more surtax)
- Corporate AMT has been repealed
- Dividends received deduction reduced 70% to 50% and 80% to 65%

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## 20% Pass-through Deduction

- 20% of qualified business income deduction (QBIID)
- Qualified business income definitions
  - Qualified trade/business income
    - Not a specified trade/business
    - Trade/business involving performance of services (law, Medicine, consulting, CPA, etc...)
  - Does not include investment income
  - Does not include reasonable compensation paid from S corporation or guaranteed payments paid to a partner
  - Phaseout limitation based on filing status and income

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## Partnership Change

- Repeal of technical termination provisions
- Greater than 50% ownership change (12 mos.)
  - No longer an automatic termination
  - No need to “close the books”
  - No short year returns
  - Effective for years after 12/31/17

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## Depreciation

- Additional first year/bonus depreciation-100% for property acquired after 9/27/17
- Phase down schedule for years after 2022
- Now allowed for new and used property
- Qualified improvement property – new definition and recover life
- Luxury auto limits – (note that additional \$8k depreciation has been extended for 2017)
- Increases to Sec. 179 (\$1M and threshold \$2.5M)
- Sec 179 can't create or increase a loss
- Limits are indexed for inflation
- Expansion for certain real property (roofs, HVAC) this is a permanent change
- Allows 179 for residential rental property

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## Accounting Methods for Small Taxpayers

- Expanded availability of cash method (< 25,000,000)
- Inventory tracking requirements (< 25,000,000)
- Sec. 263A threshold raised (< 25,000,000)
- Expanded availability of completed contract method (< 10,000,000)

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## Changes to Fringe Benefits/Entertainment Expense

- Repeal of business entertainment expenses
- Repeal of deduction for qualified transportation fringe benefits
- Repeal of exclusion for bicycle commuting reimbursement
- Repeal of exclusion for employee reimbursed moving expenses
- Other changes to employee fringe benefits

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## Net Operating Loss Provisions

- No longer allowed to carryback NOLs
- Carried forward indefinitely
- 80% of taxable income may be reduced by NOL
- Exclusions for Farmers and Extraordinary Circumstances (i.e. Harvey)

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## Other changes to note:

- Changes for Sec. 1031 exchanges
- Expenses for employer operating eating facilities is now 50% (rather than fully deductible)
- Lobbying costs no longer deductible
- New credit for paid family and medical leave

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## Planning for 2019 and Beyond

- Guidance needed on Sec. 199A (pass-through deduction)
  - Definitions: qualified business income; qualified trade/business; small business
- Effect of corporate rate reduction to 21% on choice of entity
- Debt structure due to interest limitations
- Entertainment expenses
- Changes to fringe benefits and effect on employees

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## International Changes

- Move to a quasi-territorial system with a 100% dividends received deduction
- One-time tax on previously unrepatriated earnings
- Other significant changes for international tax law



## MORE Many Individual changes!

- Generally effective after 12/31/17
- Most changes are temporary
  - Sunset after 2025
- Guidance is needed
- Future legislation? Watch out!
- State conformity to changes?

## The Basics

- Still seven tax brackets
  - 10%, 12%, 22%, 24%, 32%, 35%, 37%
- No more dependent exemption
- Higher child tax credit (\$2,000) phase out at 400,000
  - New \$500 non-child dependent credit
- Increase in standard deduction ((12,000 – 24,000) and increases to 12,400 in 2019)
- Individual AMT not repealed
  - But exemption amounts have increased from 78,750 to 109,400

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## Individual Tax Rates (MFJ)

<u>2018</u>	<u>RATE</u>	<u>2019</u>
0-19,050	10%	0-19,400
19,051-77,400	12%	19,401-78,950
77,401-165,000	22%	78,951-168,400
165,001-315,000	24%	168,401-321,450
315,001-400,000	32%	321,451-408,200
400,001-600,000	35%	408,201-612,350
600,001+	37%	612,351+

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## Dividend and Capital Gains Rates Unchanged

- The top tax bracket for qualified dividends and capital gains is 20% (23.8% if the net investment income tax applies).

Here's the breakdown:



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## Retirement Plan Contributions Limits

	2018	2019
	18,500	19,000
	6,000	6,000
	5,500	6,000
	1,000	1,000
	12,500	13,000
	3,000	3,000
	55,000	56,000
	275,000	280,000

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## 20% Pass-through Deduction

- 20% of qualified business income
- Qualified business income definitions
  - Qualified trade/business income
    - Not a specified trade/business
      - Trade/business involving performance of services
  - Does not include investment income
- Does not include reasonable compensation paid from S corporation or guaranteed payments paid to a partner
- Phase-out limitation

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## Itemized Deductions Changes

- Repeal of the overall limitation on itemized deductions
- Medical deduction threshold is 7.5% for 2017 & 2018
  - Reverts to 10% starting in 2019
- Mortgage interest limited to \$750k of debt
  - Debt prior to 12/15/17 is grandfathered
- Home equity interest no longer deductible (additions ??)
- State and local tax deduction is limited to \$10k
- Misc. deductions subject to 2% threshold no longer deductible

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## Charitable Contribution Changes

- AGI limitation increased to 60% for cash contributions (from 50%)
- No 80% deduction for right to purchase athletic tickets
- Exception to contemporaneous written acknowledgement requirement is repealed (must be obtained now for any contribution of \$250 or more)
- \$.14 a mile deduction

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## State and Local Tax Issues

- Total deduction limit of \$10k (\$5k if MFS)
  - Combination of income/sales and state/local property taxes
- Exceptions
  - Tax imposed at entity level
  - Property taxes for residential rental property/business property

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## Misc. Itemized Deductions Subject to 2% AGI

- Unreimbursed employee expenses
- Tax prep fees
- Hobby expenses
- Investment fees/expenses
- Legal fees related to producing income
- Safe deposit fee

*...are no longer deductible*

**YIKES!!!**

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## Other Individual Changes to Note:

- Casualty losses: only from federally-declared disasters
- Alimony: deduction/inclusion repealed for divorces executed after 12/31/18
- Moving expenses deduction repealed
- Kiddie tax now at trusts/estate tax rates
- Medical expense exceed 10% of AGI

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## Depreciation Changes

- Additional first year/bonus depreciation- 100% for property acquired after 9/27/17
- Phase down schedule for years after 2022
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- Qualified improvement property no longer qualifies
- Luxury auto limits – (note that additional \$8k depreciation has been extended for 2017)
- Increases to Sec. 179 (\$1M and threshold \$2.5M)
- SUV limitation remains at \$25,000
- Limits are indexed for inflation
- Expansion for certain real property (roofs, HVAC)
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## Affects on the net investment income tax (NIIT)

- No change to NIIT itself, but.....
- Investment fees and state income tax (amount attributable to investment income) reduce investment income to lower amount subject to NIIT
- Since investment fees are no longer deductible and state income tax is limited to \$10k, this will likely cause an increase in the amount subject to NIIT

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## Alternative Minimum Tax (AMT) changes

- Alternative tax system that parallels the regular federal tax (with different rates and rules for deductions)
- Increase in exemption amount
- Due to limit on state/local tax deduction and repeal of miscellaneous deductions, impact should be less

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## Estate and Gift Taxes Changes

- 2018 estate tax exemption: \$11.2 million, 11.8 for 2019
- 2019 gift tax annual exclusion: \$15,000
- Estate planning is more than minimizing estate taxes.
  - Updating documents
  - Repurposing insurance
  - Privacy
  - Asset protection
  - Exemption portability

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## Education Tax Benefit Changes

- Sec 529 plan distributions for private school tuition
- Sec 529 plan assets can transfer to ABLER accounts for family members
- Student loan forgiveness will not be taxable income to student upon death/total disability





## Affordable Care Act Impact

- Penalty to maintain insurance coverage (individual mandate) is repealed for 2019 and forward
- HOWEVER, still in effect for 2017 and 2018
- 2017 penalty:
  - Higher of 2.5% of yearly household income, or
  - \$695 per person (\$347.50 per child under 18)

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## Plan now to avoid underpayment penalties

- Estimated tax payments/withholding
- New W-4 released in July – August 2019

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## Proposed changes not included in final bill (but were in either House or Senate bill) include ...

- Additional standard deduction for elderly and blind
- \$250 above-the-line teacher deduction is not changed
- Exclusion for employer-provided dependent care assistance
- Exclusion for adoption assistance programs
- Reduction of capital gain rates/changes to taxation of interest income
- Sec. 121 exclusion of gain on sale of principal residence
- Required use of FIFO to determine basis of stock dispositions
- Charitable driving remains at 14 cents/mile (rather than actual)
- Consolidation and modification of education provisions not included (only change is to expand 529 plans)
- Plug-in electric vehicle credit (Sec. 30D)

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## Planning Opportunities

Complexity = possible savings opportunities

Consider evaluating tax structure

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## Planning tips

Requires rethinking and planning in many areas

- Choice of entity for business ventures
- Charitable giving planning
- Estate/gift planning with temporary increased exemption
- Stock option and restricted stock exercise planning
- Interplay of Sec. 199A with remaining rules such as NIIT, passive activity loss limits

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# Thank you

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