



BDO KNOWS: TAX REFORM

PLANNING FOR TAX REFORM

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Planning for Tax Reform Introduction and Today's Agenda

Matt Becker



Agenda

- ▶ The Path to Tax Reform and What's Next - Todd Simmens
- ▶ Individual - Jack Nuckolls
- ▶ Not for Profit - Laura Kalick
- ▶ Partnerships and Pass Through Entities - Jeff Bilsky
- ▶ Corporate - Ben Willis
- ▶ Research and Orphan Drug Credit and DPAD - Chris Bard
- ▶ International - Joe Calianno
- ▶ Compensation and Benefits - Pete Klinger
- ▶ Accounting Methods and Cost Recovery - Dave Hammond
- ▶ Accounting for Income Taxes (ASC 740) - Yosef Barbut

Disclaimer: Today's webcast is intended to provide a high level overview of certain provisions contained in the new tax law and is not intended to be a comprehensive discussion. For application of the new law to specific cases, a tax advisor should be consulted.

Path to Tax Reform and What's Next

Todd Simmens



Path to Tax Reform

- ▶ Tax reform: A priority of this and prior Congresses
- ▶ Concepts and framework have been brewing for several years
- ▶ 10-year Senate Reconciliation rules becoming a major factor in tax legislation



What's Next

- ▶ IRS has its work cut out
 - With a year reprieve for most provisions
- ▶ Regulatory and other guidance
- ▶ Joint Committee on Taxation Bluebook
- ▶ Technical corrections
- ▶ Planning for the 10-year sunset of most provisions



Individual Tax

Jack Nuckolls



Introduction-Individual Provisions

- ▶ In general, the individual provisions go into effect starting on January 1, 2018, but are set to expire on December 31, 2025.

Estate, Gift, and Generation-Skipping Transfer Taxes

- ▶ Estate and Gift Taxes - Beginning in 2018, the exemption for estate and gift taxes is increased to \$10,000,000 (and adjusted forward for inflation from 2011).
 - *Inflation - There will be a roughly \$11,000,000 estate and gift exemption starting in 2018.*

- ▶ Generation-Skipping Transfer Tax - Beginning in 2018, the amount of the generation-skipping transfer tax exemption is increased to \$10,000,000 (and adjusted forward for inflation from 2011).
 - *Inflation - There will be a roughly \$11,000,000 generation-skipping transfer tax exemption starting in 2018.*
 - ▶ These increases are set to expire on December 31, 2025, and the exemption amounts will return to the pre-tax reform amounts.
 - *This makes the current planning techniques still relevant, even for estates that do not exceed the increased exemption amount.*

Ordinary Income Tax Rates

- ▶ The current seven tax bracket system is retained, but the rates are lowered for all taxpayers and the thresholds are adjusted below.

Tax Rate	Married Filing Jointly and Surviving Spouses	Single	Head of Household	Married Filing Separately	Estates & Trusts
10%	\$0 - \$19,050	\$0 - \$9,525	\$0 - \$13,600	\$0 - \$9,525	\$0 - \$2,550
12%	\$19,050 - \$77,400	\$9,525 - \$38,700	\$13,600 - \$51,800	\$9,525 - \$38,700	N/A
22%	\$77,400 - \$165,000	\$38,700 - \$82,500	\$51,800 - \$82,500	\$38,700 - \$82,500	N/A
24%	\$165,000 - \$315,000	\$82,500 - \$157,500	\$82,500 - \$157,500	\$82,500 - \$157,500	\$2,550 - \$9,150
32%	\$315,000 - \$400,000	\$157,500 - \$200,000	\$157,500 - \$200,000	\$157,500 - \$200,000	N/A
35%	\$400,000 - \$600,000	\$200,000 - \$500,000	\$200,000 - \$500,000	\$200,000 - \$300,000	\$9,150 - \$12,500
37%	Over \$600,000	Over \$500,000	Over \$500,000	Over \$300,000	Over \$12,500



Kiddie Tax

- ▶ Children that are subject to the “Kiddie Tax” will have two different tax regimes for their earned and unearned income:
 - Earned Income: Taxed at the rates applied to single filers.
 - Unearned Income: Taxed at ordinary income and preferential rates applied to trusts and estates.
 - ▶ *Children will no longer be subject to their parents’ tax rate.*

Above-the-Line Deductions

- ▶ Moving Expenses - Suspended through tax year 2025; however, still available for members of the U.S. military who move pursuant to a military order.

- ▶ Alimony - Effective for divorce or separation agreements entered into after December 31, 2018*:
 - Deduction - The deduction for alimony or separate maintenance payments is repealed.
 - Inclusion - The inclusion of income by the recipient is repealed.
 - ▶ *Existing alimony or separate maintenance agreements are grandfathered, as are modifications to existing agreements.*
 - **Please note the 1-year delay on the implementation of this provision*

Standard Deduction & Personal Exemptions

- ▶ The standard deduction is increased to the following amounts:
 - Married Filing Jointly: \$24,000
 - Head-of-Household: \$18,000
 - All Other Taxpayers: \$12,000
 - ▶ *The deduction is indexed for inflation in future years.*

- ▶ The personal exemption is suspended through tax year 2025.
 - The personal exemption for estates and trusts remains at \$100 (complex), \$300 (simple), \$600 (estates).

Itemized Deductions

- ▶ Medical Expenses - The AGI threshold is lowered to 7.5 percent for all taxpayers for tax years 2017 and 2018.
- ▶ State and Local Taxes - Taxpayers are permitted a maximum \$10,000 deduction on the sum of:
 - (i) state and local real property taxes,
 - (ii) state and local personal property taxes, and
 - (iii) state and local income taxes (or sales tax, if elected).
 - ▶ *This limitation does not apply to real property taxes and personal property taxes paid or accrued in carrying on a trade or business.*
- ▶ Mortgage Interest - Taxpayers are permitted to deduct the interest paid on acquisition indebtedness of up to \$750,000.
 - *Debt incurred on or before December 15, 2017, is grandfathered under the previous law of interest paid on acquisition indebtedness of up to \$1,000,000.*
- ▶ Home Equity Interest - The deduction for interest paid on home equity indebtedness is suspended.

Itemized Deductions (Continued)

- ▶ Charitable Contributions - Three modifications:
 - (1) Cash contributions to public charities now have a 60 percent of AGI limitation (previously it was 50 percent).
 - (2) Denial of charitable deduction for payments made in exchange for athletic seating rights (previously able to deduct 80 percent of amounts paid).
 - (3) Removal of substantiation exception for certain contributions reported by the charitable organization.
- ▶ Casualty Losses - Suspended through tax year 2025, unless the loss is attributable to a Federally declared disaster loss.
 - *If a taxpayer has a personal casualty loss gain, they may deduct personal casualty losses not attributable to a Federal declared disaster loss in the amount equal to no more than the personal casualty loss gain.*
- ▶ Wagering Transactions - In addition to the limitation on gambling losses, expenses incurred in carrying on any wagering transaction are also limited to the extent of gambling winnings.



Itemized Deductions (Continued)

- ▶ Miscellaneous Itemized Deductions Subject to 2-percent floor - These have been suspended and include investment fees and expenses, tax preparation fees, and unreimbursed business expenses, among others.
- ▶ “Pease” Limitation - Repeals the overall limitation on itemized deductions through 2025.

Alternative Minimum Tax (AMT)

- ▶ The individual AMT has been retained.
 - The exemption amounts have been increased to the following thresholds:
 - Joint Filers: \$109,400 (\$54,700 for MFS)
 - All other Filers: \$70,300
 - The exemption phase-out thresholds are increased to:
 - Joint Filers: \$1,000,000
 - All other Filers: \$500,000
 - Trusts and Estates - Remains unchanged.
 - *Many of the tax preference items that are AMT addbacks have been suspended.*

Business Losses

- ▶ Businesses Losses - Business losses are only permitted in the current year to the extent that they do not exceed the sum of:
 - (i) Taxpayer's gross income and
 - (ii) \$500,000 for joint filers or \$250,000 for other taxpayers
 - ▶ Excess businesses losses will be disallowed and added to the taxpayer's net operating loss (NOL) carryforward.
 - Carryforwards are limited to the lesser of:
 - (i) the carryforward amount or
 - (ii) 80-percent of taxable income determined without regard to the NOL deduction.
 - ▶ *For pass-through entities, this is applied at the partner/shareholder level.*

Net Operating Losses

- ▶ Net Operating Losses - The deduction allowed is now equal to the lesser of:
 - (1) the aggregate of the net operating loss carryovers to such year, plus the net operating loss carrybacks to such year, or
 - (2) 80 percent of the taxable income computed without regard to the NOL.
 - ▶ *NOLs can now only be carried forward to future tax years.*
 - The amount of the carryover is limited to a maximum of 80 percent of the taxable income computed without regard to the NOL.



Not for Profit Tax

Laura Kalick



Charitable Giving

- ▶ **Reduces Incentives for Charitable Giving by:**
 - Doubling the Standard Deduction
 - Doubling Estate Tax Exemptions
 - Repealing the deduction for Tickets to College Athletic Events

- ▶ **Increases the Incentives for Charitable Giving by:**
 - Repealing the “Pease” Limitation
 - Increasing the Charitable Contribution Deduction Limit



Excise Taxes

▶ Executive Compensation

The Act imposes a 21-percent excise tax on the compensation of the five highest compensated employees with compensation in excess of \$1 million. There is an exception for certain medical professionals.

▶ College and University Endowment Tax

Imposes a tax of 1.4-percent on the net investment income of a college or university which had at least 500 tuition-paying students during the preceding taxable year and the aggregate fair market value of the assets (other than those assets which are used directly in carrying out the institution's exempt purpose) is at least \$500,000 per student of the institution.



Unrelated Trade or Business Income

▶ UBIT Losses

The bill disallows tax-exempt organizations from taking the business losses from one unrelated activity and deducting them from the gains of another unrelated activity. Organizations could, however, use losses from an unrelated business to reduce taxes on another year's operation of the same unrelated business.

▶ Inclusion of Certain Fringe Benefits in UBTI Calculation

Unrelated business income of a tax-exempt organization would be increased by amounts spent by the organization on qualified transportation fringe benefits, parking facilities, and onsite athletic facilities.

Taxation of Partnerships and Pass Through Entities

Jeff Bilsky



Provisions Impacting Partnerships and Pass Through Entities

- ▶ Section 199A Deduction for Qualified Business Income
- ▶ Recharacterization of Certain Long-Term Capital Gains
- ▶ Other Partnership-Related Provisions
 - Taxation of Gain on the Sale of Partnership Interest by Foreign Person
 - Repeal of Technical Termination Rules under Section 708(b)(1)(B)
 - Modification of the Definition of Substantial Built-in Loss under Section 743(d)
 - Section 704(d) Basis Limitation: Charitable Contributions & Foreign Taxes
 - Like-Kind Exchange Transactions under Section 1031

Section 199A Deduction for Qualified Business Income

- ▶ Taxpayers other than corporations are generally eligible to claim a deduction equal to the sum of:
 - 1) The lesser of (A) the taxpayer's "combined qualified business income amount" or (B) 20 percent of the excess of the taxpayer's taxable income over capital gain plus qualified cooperative dividends, plus
 - 2) The lesser of (A) 20 percent of the aggregate amount of qualified cooperative dividends or (B) the taxpayer's taxable income (reduced by net capital gains)
- ▶ A taxpayer's combined qualified business income amount is equal to the sum of (1) 20 percent of the taxpayer qualified business income (QBI) with respect to each qualified trade or business plus (2) 20 percent of the aggregate amount of qualified real estate investment trust dividends and qualified publicly traded partnership income

Section 199A Deduction for Qualified Business Income

- ▶ QBI includes the net amount of domestic qualified items of income, gain, deduction, and loss with respect to the taxpayer's qualified businesses
- ▶ Qualified trade or business includes any trades or businesses other than specified service trades or businesses
- ▶ A specified service trade or business means any trade or business involving the performance of services in the fields of:
 - Health, law, accounting, actuarial sciences, performing arts, consulting, athletics, financial services, brokerage services, 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
- ▶ Exception for specified service businesses where a taxpayer's taxable income does not exceed \$315,000 (joint filer) or \$157,500 (other filers), subject to full phase-in at \$415,000 and \$207,500, respectively

Section 199A Deduction for Qualified Business Income

Limitation

- ▶ The deduction attributable to 20 percent of the taxpayer's QBI cannot exceed the greater of (A) 50 percent of W-2 wages paid with respect to the QBI or (B) The sum of 25 percent of W-2 wages plus 2.5 percent of the unadjusted basis of qualified property
- ▶ Qualified property includes depreciable tangible property that is (i) held by and available for use in the trade or business at the close of the taxable year, (ii) used during the year in the production of QBI, and (iii) has a remaining depreciable period
- ▶ The term "depreciable period" means the later of 10 years from the original placed in-service date or the last day of the last full year in the applicable recovery period determined under section 168
- ▶ The W-2 wages or W-2 wages plus capital limitation does not apply to taxpayers with taxable income not exceeding \$315,000 (joint filers) or \$157,500 (other filers). The limitation is phased-in for taxpayers with taxable income exceeding these amounts over ranges of \$100,000 and \$50,000

Recharacterization of Certain Capital Gains

- ▶ Gain on sale of capital assets held more than 1-year generally subject to long-term capital gain rates
- ▶ Gain attributable to “applicable partnership interests” is subject to recharacterization as short-term capital gain unless the underlying asset has been held for at least 3 years
- ▶ Applicable partnership interests include partnership interests that are transferred to (or held by) the taxpayer in connection with the performance of substantial services in any “applicable trade or business”
 - Applicable trade or business includes an activity (1) conducted on a regular, continuous and substantial basis, (2) consists of raising or returning capital, and (3) either investing in (or disposing of) specified assets or developing specified assets
 - Specified assets include securities and commodities, real estate held for rental or investment, cash or cash equivalents, options or derivative contracts on any of the above, or proportionate partnership interests in any of the above
 - Applicable partnership interests do not include interests that are held directly or indirectly by a corporation or capital interests that provide a right to share in capital commensurate with (a) amount of capital contributed or (b) value of such interest subject to tax under section 83 upon the receipt of vesting of such interest



Other Partnership-Related Provisions

- ▶ Taxation of Gain on the Sale of Partnership Interest by Foreign Person
- ▶ Repeal of Technical Termination Rules under Section 708(b)(1)(B)
- ▶ Modification of the Definition of Substantial Built-in Loss under Section 743(d)
- ▶ Section 704(d) Basis Limitation: Charitable Contributions & Foreign Taxes
- ▶ Like-Kind Exchange Transactions under Section 1031



Corporate Tax Planning

Ben Willis



Corporate Tax Planning

- ▶ P.L. 115-97 enacted 12/22/2017 gets SEC filing concessions
- ▶ Permanent Change for C corporations
- ▶ 40-percent reduction to top rate
- ▶ Deferral for C Corporations
- ▶ Corporate tax rate reduction and AMT repeal



Corporate Tax Planning

- ▶ Capital contributions and dividends to corporations
- ▶ Debt versus equity (section 385) & new limitation on interest deductions
- ▶ Corporate net operating losses (NOLs)
- ▶ Bonus depreciation and full expensing



Corporate Tax Planning

- ▶ Section 199A deduction for qualified business income from S corporations
- ▶ Electing small business trusts (ESBTs)
- ▶ S-to-C corporation conversions
- ▶ Choice of entity

Research and Orphan Drug Credit and DPAD

Chris Bard

R&D Tax Credit

- ▶ Sec. 41's language wasn't changed
- ▶ But its R&D credit's benefit was increased for tax years beginning after 12/31/2017 thanks to changes to:
 - Corp tax rates - the rate reduction from 35 percent to 21 percent effectively increases the R&D credit's net—i.e., Sec. 280C(c)—benefit by more than 21 percent, from 65 percent to 79 percent
 - AMT - with AMT's repeal, taxpayers who would have been subject to AMT and who therefore generally would not have been able to use R&D credits to offset their federal income tax liability will be able to do so
 - NOL deductions - because taxpayers will be able to offset only 80 percent of their taxable income using NOLs generated in tax years beginning after 12/31/2017—instead of 100 percent—NOL taxpayers may be able to use R&D credits against taxes they'll now have to pay
 - Sec. 174 deduction for R&E expenditures
 - R&E expenditures paid or incurred in a tax year beginning after 12/31/2021 will no longer be able to be immediately expensed
 - Instead, they must be capitalized and amortized over a five year period beginning with the midpoint of the taxable year in which the expenditure is paid or incurred
 - Costs for research conducted outside of the U.S. will be amortized over a 15-year period
 - Expenditures for the development of any software will be treated as R&E expenditures

Sec. 45C Orphan Drug Credit & Sec. 199 DPAD

▶ Orphan Drug Credit (ODC)

- Rate reduced from 50 percent to 25 percent for tax years beginning after 12/31/2017
- Even at 25 percent, the ODC is generally more beneficial than the R&D credit for the same costs to which it applies:
 - The ODC rate is 25 percent, the R&D credit's 20 percent, or about 16 percent after Section 280C(c)
 - The ODC calculation includes 100 percent of qualified contractor costs, the R&D credit's typically only 65 percent
- The ODC rate applies to total qualified costs, the R&D credit's to only the qualified costs that exceed a base amount

▶ Sec. 199 Domestic Production Activities Deduction (DPAD)

- Repealed for tax years beginning after 12/31/2017



International Tax

Joseph Calianno

Establishment of Participation Exemption

- ▶ 100 percent DRD for certain foreign source portion of dividends received from specified 10 percent owned foreign corporations (10 percent SFCs) by U.S. C corporations (other than RICs or REITs) that are U.S. shareholders (section 951(b)) of those foreign corporations
 - A 10 percent SFC is any foreign corporation with respect to which any domestic corporation is a U.S. shareholder (such term does not include any corporation which is a PFIC with respect to the shareholder and which is not a CFC)
 - Applicable to distributions made after 12/31/17

- ▶ Reduce basis (but not below zero) in stock of 10 percent SFCs by exempt dividends (except to extent basis reduced under section 1059 by reason of such dividends) but only for purposes of determining loss on subsequent disposition of 10 percent SFC shares
 - Applicable for distributions made after 12/31/17

Establishment of Participation Exemption

- ▶ If U.S. corporation transfers substantially all of the assets of a foreign branch to a 10 percent SFC with respect to which it is a U.S. shareholder after the transfer, the U.S. corporation includes the “transferred loss amount,” subject to certain limitations
 - Applicable to transfers after 12/31/17

- ▶ Repeal of the active trade or business exception under section 367(a)
 - Applicable to transfers after 12/31/17

- ▶ Election to increase the percentage (but not greater than 100 percent) of domestic taxable income offset by any pre-2018 unused ODL and re-characterized as foreign source
 - Applicable to taxable years beginning after 12/31/17

Establishment of Participation Exemption

- ▶ U.S. shareholders (as defined in section 951(b)) of deferred foreign income corporations required to include their pro rata share of accumulated post-1986 deferred foreign income as of 11/2/2017 or 12/31/2017 (whichever is greater)
 - Deferred foreign income corporation is a specified foreign corporation (SFC) with positive accumulated post-1986 deferred foreign income on 11/2/2017 or 12/31/2017
 - SFC is (a) a CFC and (b) any foreign corporation with respect to which one or more domestic corporations is a U.S. shareholder (such term shall not include any corporation which is a PFIC with respect to the shareholder and which is not a CFC)
 - SFC described in (b) treated as CFC for purposes taking into account Subpart F income
 - Subpart F inclusion is mechanism for inclusion
 - Can apply to non-corporate U.S. shareholders
 - Deficits of certain SFCs available to reduce inclusion if certain conditions are satisfied

Establishment of Participation Exemption

- ▶ Very generally, 15.5 percent rate for E&P comprising of cash and cash equivalents/8 percent rate for E&P comprising of illiquid assets (see section 965(c) for specific details on computing rates)
- ▶ Election to pay liability in 8 installments (with amounts paid in later years increasing)
- ▶ Special rules for S corporation shareholders allowing them to elect to defer payment of tax liability until certain triggering events
- ▶ Broad regulatory authority including authority to prevent the avoidance of the purposes of the provision, including through a reduction of E&P through check-the-box elections or accounting method changes, or otherwise
- ▶ Numerous definitions and operating rules for applying provision
- ▶ Applicable for the last taxable year of a foreign corporation beginning before 1/1/18, and with respect to U.S. shareholders for tax years in which or with which such tax years of the foreign corporation end

Modifications to Foreign Tax Credit System

- ▶ Repeal of section 902 indirect FTCs for dividends; Determination of section 960 indirect FTC on a current year basis
 - Applicable to taxable years of foreign corporations beginning after 12/31/17 and to taxable years of U.S. shareholders in which or with which such taxable years end

- ▶ Sourcing for produced inventory--Sourced based solely on jurisdiction(s) of production activities under section 863(b)
 - Applicable to taxable years beginning after 12/31/17

- ▶ Foreign branch income allocated to a specific foreign tax credit basket
 - Applicable to taxable years beginning after 12/31/17

Modifications to Subpart F

- ▶ Repeal of section 955
 - Applicable to taxable years of foreign corporations beginning after 12/31/17 and to taxable years of U.S. shareholders in which or with which such taxable years end

- ▶ Eliminates foreign base company oil related income as a category of foreign base company income
 - Applicable to taxable years of foreign corporations beginning after 12/31/17 and to taxable years of U.S. shareholders in which or with which such taxable years end

- ▶ Repeals section 958(b)(4) so that certain stock of a foreign corporation owned by a foreign person is attributed to a related U.S. person for purposes of determining CFC status
 - Applicable to the last taxable year of foreign corporations beginning before 1/1/18 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

Modifications to Subpart F

- ▶ Expands the definition of U.S. shareholder to include U.S. persons who own 10 percent or more of the total value of all classes of stock of a foreign corporation
 - Applicable to taxable years of foreign corporations beginning after 12/31/17 and to taxable years of U.S. shareholders in which or with which such taxable years end

- ▶ Eliminates the requirement that a corporation be controlled for an uninterrupted period of 30 days before subpart F inclusions apply
 - Applicable to taxable years of foreign corporations beginning after 12/31/17 and to taxable years of U.S. shareholders in which or with which such taxable years end

- ▶ U.S. shareholders of any CFC must include in gross income for a taxable year “global intangible low-taxed income” in a manner generally similar to inclusions of subpart F income (new section 951A)
 - Complex formula for determining the amount
 - Applicable to taxable years of foreign corporations beginning after 12/31/17 and to taxable years of U.S. shareholders in which or with which such taxable years end

Deduction for Certain Types of Income

- ▶ Domestic C corporations (other than RICs and REITs) permitted a deduction equal to the sum of 37.5 percent of its foreign derived intangible income of the domestic corporation plus 50 percent of (i) its global intangible low-taxed income (if any) included in income by the domestic corporation under section 951A (CFC subpart F type provision) and (ii) the amount treated as a dividend received by such corporation under section 78 which is attributable to the amount in (i).
 - Limitation based on taxable income (potential reduction of deduction)
 - Special definitions in applying provision and complex calculation for determining amount
 - Percentages for deduction reduced for tax years after 2025
 - Applicable for taxable years beginning after 12/31/17

Base Erosion Provisions

- ▶ Base erosion minimum tax requires a corporation to pay additional corporate tax in situations where a corporation has certain “base erosion payments” to foreign related parties and certain thresholds and conditions are satisfied (complicated formula for determining the tax)
 - Additional tax can apply to corporate taxpayers (other than RICs, REITs and S Corporations) with annual gross receipts of at least \$500 million (three year testing period) and a “base erosion percentage” of 3 percent or more (special rules and definitions in applying test, including modification of base erosion percentage if bank or registered securities dealer part of group)
 - Applicable to base erosion payments paid or accrued in taxable years beginning after 12/31/17

- ▶ Limitations on income shifting through intangible property transfers (including treating workforce in place and goodwill and going concern value as section 936(h)(3)(B) intangibles/use of aggregate methods of valuing transfers of intangibles codified)
 - Applicable to transfers in taxable years beginning after 12/31/17



Base Erosion Provisions

- ▶ Denies a deduction for certain related party interest and royalty amounts paid or accrued pursuant to certain hybrid transactions, or by, or to, hybrid entities when certain conditions are satisfied (e.g., deduction for payor but no corresponding income inclusion in foreign jurisdiction of related party and such amount not treated as Subpart F income)
 - Broad regulatory authority
 - Applicable to taxable years beginning after 12/31/17

Other International Provisions

- ▶ Restrictions on PFIC Insurance Business Exception--the provision modifies the requirements the income of which is not included in passive income for purposes of the PFIC rules
 - Applicable to taxable years beginning after 12/31/17
- ▶ Repeal of fair market value method of interest expense apportionment
 - Applicable to taxable years beginning after 12/31/17
- ▶ Codification of Rev. Rul. 91-32--Gain or loss from the sale or exchange of a partnership interest is ECI to the extent that the transferor would have had effectively connected gain or losses had the partnership sold all of its assets at FMV as of the date of the sale or exchange
 - Rules for coordinating with FIRPTA and imposing withholding regime
 - Provision treating gain/loss as ECI is applicable for sales, exchanges and dispositions on or after 11/27/17 and provision requiring withholding is applicable for sales, exchanges and dispositions after 12/31/17



Other International Provisions

- ▶ No preferential tax rates on dividends received from a surrogate foreign corporation (section 7874(a)(2)(B)) that becomes a surrogate foreign corporation after date of enactment other than a foreign corporation which is treated as a domestic corporation under section 7874(b)
 - Applicable for dividends after date of enactment



Compensation and Benefits

Peter Klinger



Changes to Section 162(m) - \$1 Million Deduction Limitation

- ▶ Eliminates performance-based compensation deduction

- ▶ Modifies definition of “Covered Employees”
 - PEO, PFO, 3 Highest compensated officers
 - Once a covered employee, always a covered employee

- ▶ Expands “Covered Employers”
 - Publicly traded
 - Large non-listed companies with >\$10m in assets and 2,000+ shareholders
 - Foreign companies publicly traded through ADRs

Tax-Exempt Organizations: Excise Tax for Excessive Executive Compensation

- ▶ Covered Employees
 - Include the top 5 highest paid employees for the taxable year and covered employees in any prior year after 2016

- ▶ Excise tax = 21 percent x sum of:
 - Remuneration exceeding \$1 million for the taxable year; and
 - Excess parachute payments

- ▶ Excess parachute payments
 - Under rules mirroring Section 280G, separation payments would trigger excise tax if greater than 3 times the 5-year average compensation (base amount); then “excess parachute” is the amount in excess of the base amount

Qualified Equity Grants

- ▶ Employees may elect to defer the income inclusion for wages attributable to stock acquired from exercise of an option or settlement of a restricted stock unit (RSU)
- ▶ Covered Employers
 - Privately held corporations with broad-based equity plans (at least 80 percent of full-time US employees receive options and RSUs)
- ▶ Covered Employees: Full-time employees other than “Excluded Employees”
 - CEO & CFO any time; 1 percent owner in current or last 10 years (attribution rules)
 - 4 highest paid officers in current or last 10 years
- ▶ 5-year deferral period (or earlier intervening event)
 - IPO, revocation of election, becoming an Excluded Employee

Retirement Plans

- ▶ Plan loan offsets
 - For participants who terminate with outstanding loans, loan is offset by reducing vested account balance
 - Participant may defer taxation on loan by rolling over and contributing balance to IRA
 - Timeline for making rollover is extended from 60 days after the offset to the due date (including extension) of income tax return for year of offset

- ▶ 2016 disaster relief - qualified distributions
 - Distributions during 2016-2017 not exceeding \$100,000
 - Avoids 10 percent early withdrawal tax
 - May include in income ratably over 3-year period from date of distribution
 - Ability to recontribute all or a portion during 3-year period



Fringe Benefits

- ▶ Achievement awards
 - Clarifies cash & equivalents and non-tangible property (e.g., theatre tickets) awarded for long service/safety achievement are included in income

- ▶ Qualified bicycle commuting reimbursements
 - Suspends exclusion from gross income for periods for 1/1/2018 - 12/31/2026

- ▶ Qualified transportation fringe benefits
 - No employer deduction (except employer-provided transportation for safety)

- ▶ Qualified moving expenses (employer-paid)
 - Suspends exclusion for 1/1/2018 - 12/31/2026

Entertainment & Meal Expenses

- ▶ Entertainment expenses
 - No deduction for entertainment, or recreation activities, facilities, or membership dues related to such activities
 - Repeals the “directly-related-to” and “associated-with” exceptions to the deduction disallowance
 - Deduction allowed for amount included in employee’s income
- ▶ 50 percent deduction limitation for meals
 - Entertainment meals are non-deductible
 - Deduction for meals provided on or near employee’s premises for convenience of employer reduced from 100 percent to 50 percent
 - Meals incurred on business travel are 50 percent deductible

Employer Credit for Paid Family and Medical Leave

- ▶ Allows employers to claim a credit equal to 12.5 percent of the amount of wages paid to employees during a family and medical leave
 - Pay must be at least 50 percent of wages normally paid to the employee
 - Credit is increased 0.25 percent (up to 25 percent) for each 1 percent by which the rate of pay exceeds 50 percent
 - 12 weeks maximum duration each taxable year
- ▶ Any leave which is paid by a state or required by state law will not be taken into account in determining the amount of paid family and medical leave provided by the employer
- ▶ Program sunsets on December 31, 2019



Affordable Care Act

- ▶ Reduces penalty for Individual Mandate to \$0 effective 2019

- ▶ Indirect impact on employers
 - Employers with self-insured plans should no longer be required to report persons covered under plan each month (employees, spouse & dependents)
 - Full-time employees may drop employer coverage
 - Full-time employees may drop Exchange coverage, reducing threat of penalty if such employees qualify for federal subsidy

Accounting Methods and Cost Recovery

Dave Hammond

Accounting Methods

Notable Tax Reform Provisions

▶ Section 451

- An accrual basis taxpayer is now required to recognize an item into income no later than the year in which the item is taken into account on the applicable financial statement.
 - An accrual method taxpayer with an applicable financial statement (AFS) would include an item in income under section 451 upon the earlier of when the all events test is met or when the taxpayer includes such item in revenue in an applicable financial statement.
- The 1-year deferral method of accounting for advance payments for goods, services, and other specified items under Rev. Proc. 2004-34 is now codified.

▶ 100 percent Bonus Depreciation

- Full expensing for the section 168(k) property placed in service after September 27, 2017 for a five-year period
- Applies for both new and used property

▶ New \$25M Threshold for Small Taxpayers

- Expands ability to use overall cash method of accounting
- Exception from requirement to keep inventory and UNICAP

Accounting Methods

Temporary and Permanent Benefit from Corporate Tax Rate Reduction

- ▶ Changing to an optimal method of accounting generally provides only a timing (or temporary) benefit; however, changing a method of accounting prior to a rate reduction can also yield a permanent tax savings benefit.
- ▶ For example, assume accrual basis C corp (TP) receives advance payments of \$1M in 2017, of which 100 percent is treated by GAAP as deferred revenue into 2018. TP has historically used the full inclusion method for recognizing advance payments for tax. TP files an auto Form 3115 to change to the 1-year deferral method for 2017. Apart from the section 481(a) adj., the \$1M is deferred into 2018 when the rate is reduced:

	Full Inclusion (No Methods Planning)	Deferral (With Methods Planning)
Income Inclusion	1,000,000	1,000,000
Tax Rate	<u>35 percent</u>	<u>21 percent</u>
Tax Liability	\$350,000	\$210,000

- ▶ Accelerating deductions into 2017 when rates are higher similarly generates a permanent tax benefit.

Accounting Methods

Top Taxpayer-Favorable Methods

▶ Income Recognition

- Deferral of advance payments for goods, services, eligible gift cards, etc. (1-year deferral method)*
- Deferral of retainages*
- Revenue recognition upon acceptance/delivery
- Overall accrual to cash method of accounting
- Nonaccrual-experience method *

▶ Expense Recognition/Capitalization

- Impermissible to permissible depreciation and amortization*
- Software development costs*
- Recurring item exception for taxes, insurance, rebates, etc.*
- Prepaid expenses under the 12-month rule*
- Self-insured medical expenses (IBNR)*
- Remodel-refresh safe harbor*
- Cash to accrual for specific items*

* Automatic Change

Accounting Methods

Procedures for Filing Form 3115

Generally, a Form 3115, *Application for Change in Accounting Method*, is required

- ▶ Two types of method changes: automatic and non-automatic (i.e., advance consent); generally, automatic changes are easier to implement

	Automatic	Non-Automatic
Revenue Procedure	2017-30 / 2015-13	2015-13
Due Date	Tax return due date (incl. extensions) for year of change	Last day of year of change
Filing Fee	None	\$9,500+
Filing Requirements	File copy with IRS in Covington, KY; attach original to return	File original with IRS National Office in Washington, DC
Consent	Deemed consent	IRS National Office must issue consent agreement

Accounting for Income Taxes (ASC 740)

Yosef Barbut



ASC 740 – Tax Reform Overall Implications

- ▶ New tax rules introduce new ASC 740 complexities & challenges
- ▶ Potential changes in supply chain and asset holdings
- ▶ Increase restructuring and planning (e.g. tax status change)
- ▶ Tax regulations forthcoming
- ▶ More ASC 740 guidance forthcoming
 - SEC/FASB/Accounting Firms Working Groups



ASC 740 - Enactment Period

- ▶ Enactment date (December 22, 2017)
 - U.S. GAAP and IFRS
- ▶ Enactment period accounting
- ▶ SAB 118 guidance



ASC 740 - SAB 118 Guidance

- ▶ SEC staff interpretations
- ▶ Measurement period approach
- ▶ Incomplete accounting
- ▶ Reasonable estimate/completed accounting
- ▶ Disclosure requirements
- ▶ Further guidance: *See BDO SEC Flash Report No. 2017-13*



ASC 740 - Remeasurement of Deferred Taxes

- ▶ New applicable rate of 21 percent
- ▶ Adjustment to income tax expense (discrete interim period)
- ▶ Remeasurement complexities (calendar vs. fiscal year)
- ▶ Intraperiod allocation
- ▶ State deferred taxes corollary effect
- ▶ Valuation allowance corollary effect



ASC 740 – Final U.S. Tax on Accumulated Foreign Earnings

- ▶ Recognition period (enactment period)
- ▶ Measurement (many variables + accumulated translation effects in OCI)
- ▶ Balance sheet presentation & classification
- ▶ Uncertain tax positions (assertions/positions impacting final tax)
- ▶ Valuation allowance impact (final tax source of income)
- ▶ State and local impact



ASC 740 - Other Provisions

- ▶ Alternative Minimum Tax (“AMT”)
- ▶ Net Operating Loss (“NOL”) deduction limitation and carryforward period
- ▶ Net interest expense deduction limitation
- ▶ Base Erosion and Anti-abuse Tax (“BEAT”)
- ▶ Global Intangible Low-taxed Income (“GILTI”)
- ▶ Deduction for Foreign Derived Intangible Income (“FDII”)

Conclusion



Questions?

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