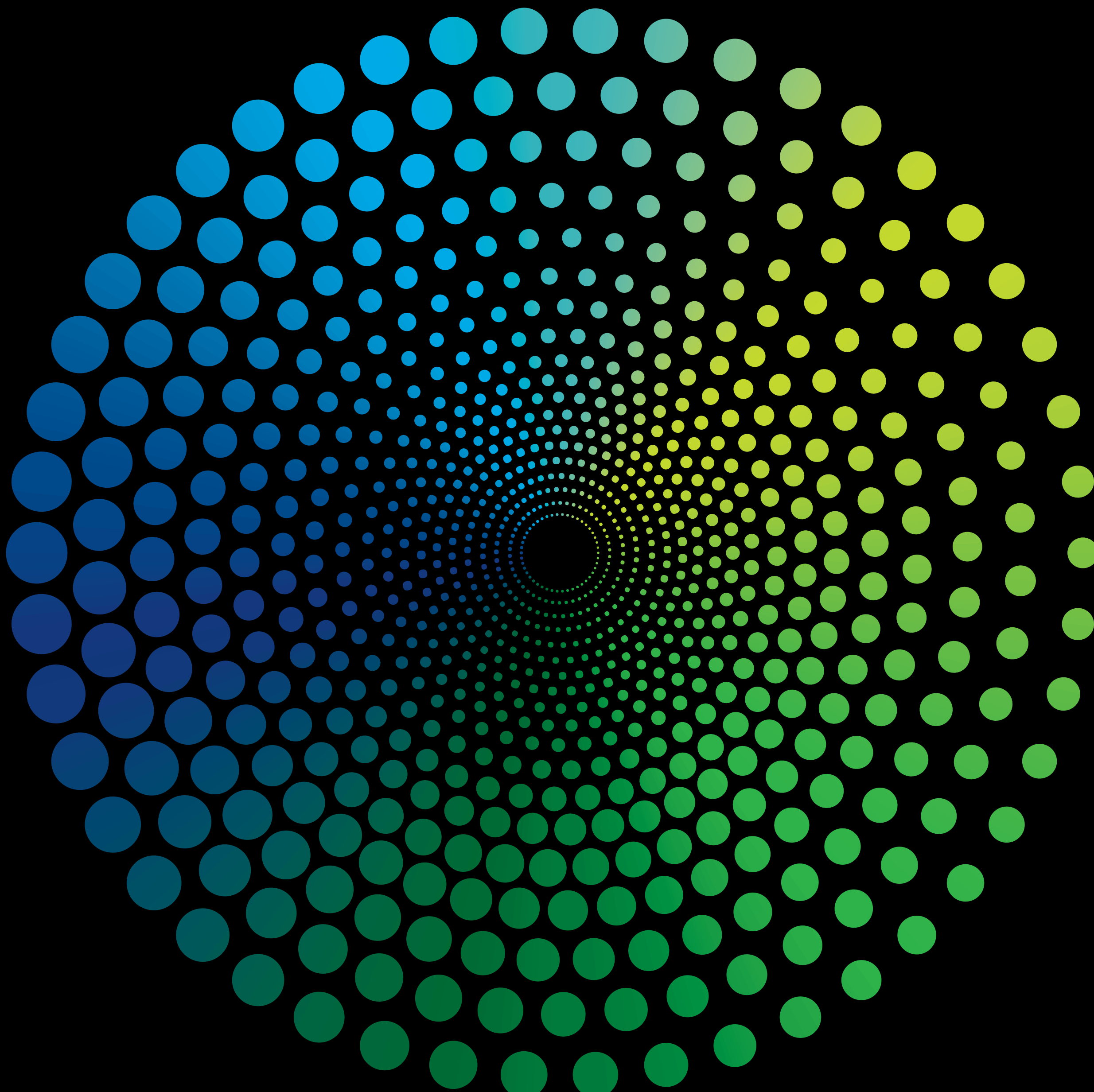


Reshaping the code:
Understanding the new tax reform law

Contents

Introduction

Congress has approved and President Trump has signed into law a massive tax reform package that lowers tax rates on corporations, pass-through entities, individuals, and estates and moves the United States toward a participation exemption-style system for taxing foreign-source income of domestic multinational corporations, with some of the cost of that tax relief offset by provisions that scale back or eliminate many longstanding deductions, credits, and incentives for businesses and individuals. The unoffset costs—roughly $1.46 trillion for the 10-year budget window covering 2018–2027, according to a revenue estimate from the Joint Committee on Taxation (JCT) staff—will be added to the deficit.

The legislation was approved in the House of Representatives and the Senate on December 20, 2017. As expected, the floor votes in both chambers were a partisan exercise. House and Senate Democrats remained in lockstep against the legislation, but Republicans mustered enough votes from within their own ranks to ensure success.

The president signed the measure into law on December 22, 2017.

Overview

The newly enacted law, officially known as *An Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018* (the Act), is an amalgam of two competing tax reform measures—one approved in the House on November 16, 2017, and the other approved in the Senate on December 2, 2017—although in some significant ways it tracks more closely with the Senate bill.

That outcome is a likely nod to several factors—most notably, the fact that the legislation moved through Congress under budget reconciliation protections that allow certain legislation to clear the Senate with a simple majority vote rather than the three-fifths supermajority required to overcome procedural hurdles that normally arise in that chamber. Those protections come with a price, however, including strict budgetary and procedural rules—the so-called Byrd Rules—that, among other things, prohibit reconciliation legislation from increasing the federal budget deficit outside the 10-year budget window and make it more difficult for lawmakers to include provisions that have no impact or only an incidental impact on the federal budget.

Another significant factor in play was GOP's narrow margin of control in that chamber—a mere four seats in 2017—which left Senate Republican leaders with little margin for error in securing final passage.

Here are just a few of the highlights of the new law:

- **Corporations**—The Act replaces the prior-law graduated corporate rate structure with a flat 21 percent rate, effective in 2018 and fully repeals the corporate alternative minimum tax (AMT). It also permits items that are amortized under current law to be fully expensed in the year placed in service through 2022, with a phaseout of that benefit thereafter. On the offset side, it imposes new limits on the deduction for net business interest, repeals the section 199 manufacturing deduction and the deduction for state and local lobbying expenses, and disallows like-kind exchanges other than for real property.
- **Pass-throughs**—The Act allows a deduction of up to 20 percent of pass-through income, although the deduction is only available for owners of specified service businesses with income under $157,500 (twice that for married filing jointly) and the definition of "specified service" no longer includes architecture or engineering. The deduction is available to electing small business trusts (ESBTs) as well as individuals, and owners are allowed to calculate their maximum deduction based on either 50 percent of their share of W-2 wages paid or a combination of 25 percent of their share of W-2 wages paid plus 2.5 percent of the unadjusted basis of all qualified property. Carried interest income retains its treatment as a capital gain, although it will be subject to a longer holding period (three years as opposed to one year in prior law) in order to qualify for lower long-term capital gains rates.
- **International**—The Act moves the United States from a worldwide tax system to a participation exemption system by giving corporations a 100 percent dividends received deduction for dividends distributed by a controlled foreign corporation (CFC). To transition to that new system, the Act imposes a one-time deemed repatriation tax, payable over eight years, on unremitted earnings and profits at a rate of 8 percent for illiquid assets and 15.5 percent for cash and cash equivalents. The Act generally follows the Senate-passed structure in establishing new base erosion prevention provisions, with modifications. It does not adopt proposals in the House and Senate bills that would have made permanent the lookthrough rules for CFCs under section 954(c)(6); nor does it include a proposed new section 163(n) that would have placed a further limit on interest deductions of multinational corporations by measuring US interest expense and equity against the similar ratios for the worldwide group.
- **Individuals**—The Act generally follows the structure of the Senate-approved tax reform bill—and 2017 law—by maintaining seven individual income tax brackets. The top individual income tax rate is 37 percent (lower than in either the House or Senate bills) but includes a significant "marriage penalty." It also nearly doubles the standard deduction, repeals the current Pease limitation on itemized deductions, and expands the refundability of the child tax credit. It retains the deduction for unreimbursed medical expenses (and even offers a boost for 2017 and 2018) and leaves intact the capital gains exclusion on the sale of a primary residence in effect prior to its enactment. On the revenue side, the measure repeals personal exemptions, retains the individual AMT (albeit with higher exemption amounts), pares back the deduction for home mortgage interest (with existing mortgages grandfathered), and places substantial new limits on the ability of taxpayers to deduct state and local taxes. **As in the Senate-passed bill, almost all of the Act's individual tax changes (including all of those just mentioned) expire after 2025.**
- **Estates**—The Act generally follows the Senate-passed bill by retaining the estate tax at its current rate but doubling the exemption amounts. **As in the Senate bill, the expanded estate tax exemption amounts sunset after 2025.**

Economic growth: How much of an impact?

As already noted, the JCT staff has estimated that the Act will reduce federal revenues by roughly $1.456 trillion—within the parameters of the reconciliation instructions in the fiscal year 2018 budget resolution, which authorized a tax bill moving under budget reconciliation protections that increases the deficit by no more than $1.5 trillion over the 10-year budget window (2018–2027).

But congressional Republican leaders and White House officials contend that the economic growth resulting from tax reform will largely offset the cost of rate reductions and other tax relief over time. Congressional rules currently require the JCT and the Congressional Budget Office—the nation's other fiscal scorekeeper—to provide what are known as "dynamic" estimates, reflecting the macroeconomic impact of significant legislation, "whenever practicable." A dynamic score for the Act released by the JCT on December 22, 2017, suggests that the new law will increase economic output and generate roughly $451 billion in revenue between 2018 and 2027, with $66 billion of that amount offset by increases in federal interest payments over the same period, for a net revenue gain of $385 billion. Under that measure, the 10-year cost of the Act drops to just under $1.1 trillion.

A deeper dive . . .

Reshaping the code: Understanding the new tax reform law offers a detailed discussion of the Act and makes observations on key provisions.

The appendix to this publication includes charts showing the effective dates—and, in some cases, expiration dates—of notable business and individual provisions, as well as a series of side-by-side comparisons showing how the Act's provisions align with those in the House and Senate bills and with tax law as in effect for 2017.

Corporate and general business tax provisions

In general, the Act contains similar corporate tax provisions to the earlier versions approved in the House and Senate, and therefore does not significantly modify the current corporate tax system, which generally imposes tax on corporate income at both the entity level and the shareholder level. There will still be softening of this double-tax system due to rate reduction, however, and more fundamental changes in the cross-border context (discussed elsewhere in this publication), but without an adoption of a direct corporate integration measure. Furthermore, similar to the prior bills, transactions with respect to stock of a corporation will generally be treated the same as under current law, and the enacted legislation does not propose changes to the consolidated return provisions.

Corporate rate reduction

The Act reduces the general corporate tax rate to 21 percent for tax years beginning after December 31, 2017. It eliminates the prior brackets and the special tax rate for personal service corporations. As in the House bill (but not the Senate version), the corporate alternative minimum tax also is eliminated, with an expanded utilization of existing AMT credits against regular tax liability for tax years beginning after 2017 and before 2022, with credits also refundable in an amount equal to 50 percent (100 percent for tax years beginning in 2021) of the excess of the AMT credit for the tax year less the amount of the credit allowable against regular tax liability for that year. The Act adopts the same approach to fiscal year taxpayers as did the Senate version: Section 15 explicitly does not apply to the temporary individual rate changes under new section 1(j) and, thus, it appears that the provision will apply to the corporate rate reduction. Under section 15, a fiscal year taxpayer may obtain the benefit of the reduced corporate rate as of January 1, 2018, generally by computing a tentative tax under both rates, and then prorating the tentative tax based on number of days with and without the rate change to arrive at a "blended" tax rate.

Dividends received deduction

The Act reduces the dividends received deduction (the DRD, in general, applicable to corporate shareholders receiving a dividend from certain domestic corporations) for the 70 percent and 80 percent brackets, to 50 percent and 65 percent, respectively. The 100 percent DRD remains intact for dividends from affiliated group members. This appears to be the identical provision as in the House and Senate bills, and would generally retain the effective tax rate on such distributions at the corporate shareholder level after reducing the corporate tax rate. The DRD provision is effective for tax years beginning after December 31, 2017. There are also DRD provisions related to the international tax provisions in the Act (discussed elsewhere in this publication).

Modification of the net operating loss deduction

As in prior bills, the Act modifies aspects of prior law regarding net operating losses (NOLs). Under prior law, NOLs generally had a carryback period of two years and a carryforward period of 20 years. The Act, like earlier versions of the legislation, generally eliminates the NOL carryback period and makes the carryforward period indefinite. The amount of the NOL deduction allowed is limited to 80 percent of taxable income computed without regard to the NOL deduction, however, rather than 90 percent, as in the House version and the introductory period in the Senate version. Special rules apply to certain farming and insurance losses.

The enacted legislation does not increase the amount of NOLs by an annual interest factor, as proposed in the House bill (but not the Senate version).

Conforming amendments include, but are not limited to: (1) the repeal of carrybacks of specified liability losses defined in section 172(f) and (2) excess interest losses related to corporate equity reduction transactions under section 172(g) (the so-called CERT rules).

In general, the effective date is December 31, 2017, with the amendments to carryback and carryforward periods applying to NOLs arising in tax years ending after December 31, 2017, and with the limitation on NOL utilization (tied to 80 percent of taxable income) applying to losses arising in tax years beginning after December 31, 2017. The effective date provisions are consistent with the Senate bill but not the House version.

Limitation on business interest

Under prior law, section 163(j) limited the ability of certain corporations to deduct interest paid or accrued on indebtedness. In general, this limit applied to interest paid or accrued by certain corporations (where no US federal income tax is imposed on the interest income) whose debt-to-equity ratio exceeds 1.5 to 1.0, and where net interest expense exceeds 50 percent of its adjusted taxable income.

The Act expands the interest deductibility limitation under section 163(j) consistent with the prior bills but with certain adjustments. The general rule remains the same as compared to prior bills; the new provision generally limits the interest deduction on business interest to (1) business interest income, plus (2) 30 percent of the taxpayer's adjusted taxable income. Business interest and business interest income is defined as that allocable to a trade or business and not investment interest and income, within the meaning of section 163(d). Adjusted taxable income is computed without regard to any (1) item of income, gain, deduction, or loss, which is not allocable to the trade or business; (2) business interest income or expense; (3) any deduction allowed under section 199A (i.e., the 20 percent deduction for certain pass-through income, as described elsewhere in this publication); (4) the NOL deduction; and (5) depreciation, amortization, or depletion for tax years beginning before January 1, 2022, but taking into account depreciation, amortization, and depletion thereafter.

The limitation described above generally applies at the taxpayer level. There are special rules that apply to partnerships (more on that below). In the case of a group of affiliated corporations that file a consolidated return, the report that accompanied the conference committee agreement for the new law clarifies that the limitation applies at the consolidated tax return filing level.

For partnerships, the limitation is applied at the partnership level, with business interest expense taken in account in determining the partnership's non-separately stated taxable income or loss. A partner may also be subject to the new interest deduction limitation with respect to the partner's own business interest expense. If so, the adjusted taxable income of the partner will not include the partner's distributive share of all items of income, gain, deduction, or loss of the partnership. This avoids double counting of adjusted taxable income to allow for interest deductibility twice for the same taxable income. The partnership, however, may have excess taxable income. This excess taxable income may be taken into account by the partner in computing the partner's limitation. This allows the partner to deduct more business interest if the partnership could have deducted more business interest.

This provision generally applies to all taxpayers. It provides an exception for certain small businesses whose average annual gross receipts for the three-taxable-year period ending with the prior tax year do not exceed $25 million, and for interest allocable to performing services as an employee and businesses of certain regulated public utilities. The Act follows the Senate bill, which allows, at the taxpayer's election, a taxpayer not to apply the limitation to certain real property-related trades or businesses and certain farming businesses. There is a narrow exception for so-called "floor plan financing indebtedness" that, in general, would apply to certain financing of acquisitions for the sale or lease of certain motor vehicles.

Under the Act, business interest that is not otherwise allowed as a deduction by reason of 163(j) is treated as paid or accrued in the succeeding tax year, and may be carried forward indefinitely. Similar to prior bills, section 381(c) is amended to include disallowed business interest as a tax attribute thereunder, and section 382 is amended to treat disallowed business interest as a pre-change loss under subsection (d).

The enacted legislation removes the separate interest deduction limitation provision under section 163(n) that would have applied to certain domestic corporations that are members of worldwide affiliated groups under the prior bills (discussed elsewhere in this publication). Under those bills, taxpayers would only obtain the lesser of interest deductions allowed under new sections 163(j) and (n).

The modifications described above apply to tax years beginning after December 31, 2017.

Cost basis of specified securities

The Act did not adopt the Senate proposal to require the "first-in first-out" method for identifying specified securities sold at different dates except if otherwise allowed. Under current law, a taxpayer generally must apply a first-in first-out approach in identifying stock in a corporation acquired at different dates or at different prices, when selling or transferring some of the shares of that stock. If a taxpayer makes an adequate identification of shares of stock sold (referred to as specific identification), however, such a determination would control. Special rules apply to shares of stock in regulated investment companies (RICs) that generally permit an averaging approach. The enacted legislation does not affect current law.

Contributions to capital

The Act modifies the treatment of contributions to capital, but narrowly and not as broadly as proposed in the House-approved measure. It provides that the term contribution to capital does not include (1) contributions in aid of construction or any other contribution as a customer or potential customer, and (2) any nonshareholder contribution by any governmental entity or civic group. Thus, its application is focused on nonshareholder contributions and leaves untouched tax-free treatment for other capital contributions at the corporate transferee level, including the treatment of debt contributed to the capital of a corporate debtor. The House bill would have applied more broadly by its flush language, including revoking section 108(e)(6).

Alternative minimum tax

The Act repeals the corporate alternative minimum tax for tax years beginning after December 31, 2017. Taxpayers may claim a refund on any AMT credit carryovers—50 percent of remaining AMT credits in tax years 2018, 2019, and 2020, and a refund on all remaining credits in the tax year 2021.

Full expensing of qualified property

The Act modifies section 168 bonus depreciation to allow for full expensing of qualified property placed into service after September 27, 2017, and before January 1, 2023. Thereafter, the bonus depreciation percentage phases down annually through 2026 (80 percent in 2023, 60 percent in 2024, 40 percent in 2025, and 20 percent in 2026). Property with longer production periods and certain aircraft receive an additional year of full expensing, with phasedowns also beginning a year later. The full expensing provision also eliminates the requirement that the original use of the property begins with the taxpayer. Thus, property qualifies under this provision as long as the property was not used by the taxpayer prior to the time of acquisition.

The Act makes no changes to section 168(k)(7), which permits a taxpayer to elect out of bonus depreciation on an asset-class-by-asset-class basis.

Deductions, exclusions, income recognition

Revenue recognition: The Act requires taxpayers to recognize income no later than the taxable year in which such income is taken into account as income on the taxpayer's applicable financial statement. However, this requirement does not apply with respect to any special methods of accounting other than for certain rules involving bonds and debt instruments. The Act also codifies the deferral method of accounting for advanced payments for goods and services currently provided under Rev. Proc. 2004-34. These provisions are effective for taxable years beginning after December 31, 2017.

Like-kind exchanges of real property: The Act limits the scope of like-kind exchange nonrecognition treatment to real property not held primarily for sale. Thus, personal property that previously qualified for nonrecognition treatment no longer qualifies under the Act. The provision does not apply to any exchange where the property disposed of or received in the exchange by the taxpayer was disposed of or received before December 31, 2017.

Local lobbying expenses: The Act repeals the deduction for local lobbying expenses, which includes lobbying before Indian tribal governments. Therefore, amounts paid or incurred after the date of enactment will not be deductible. This change conforms the treatment of local lobbying expenses to that of other lobbying and political expenses, which have been and continue to be nondeductible.

Section 199 deduction: The Act repeals the section 199 deduction, effective for tax years after December 31, 2017.

Treatment of self-created property: The Act excludes patents, inventions, models or designs, and secret formulas or processes as qualifying as a capital asset under section 1221. Under prior law, these items were treated as capital assets. Under the Act, the gain or loss from the sale of a self-created patent, invention, model or design, or secret formula or process will not receive capital gain treatment. This provision is effective for disposition of such property after 2017.

Recovery period of real property: The Act eliminates the separate definitions of qualified leasehold improvements, qualified restaurants, and qualified retail improvement property, and instead provides for a single asset class called "qualified improvement property" (QIP). According to the conference report for the Act, QIP is intended to have a 15-year regular MACRS recovery period and 20-year ADS recovery period. These provisions apply to property placed in service after December 31, 2017. The Act makes no changes to the MACRS recovery period for nonresidential real and residential rental property.

Section 179 expensing: The Act increases the section 179 expense election threshold to $1 million. The phaseout of this expense election begins when the cost of qualifying property placed in service reaches $2.5 million. The Act also expands the definition of section 179 property to include certain property used in furnishing lodging, and roofs, heating, ventilation, air-conditioning property, fire protection and alarm systems, and security systems for nonresidential real property that are placed in service after December 31, 2017.

Accounting methods for small taxpayers: The Act expands the scope of eligible taxpayers who may use the cash method of accounting. It allows taxpayers with annual average gross receipts of $25 million or less to use the cash method. This gross receipt limit also applies to farming C corporations.

The Act also generally exempts taxpayers that meet the $25 million gross receipts test from the requirement to keep inventories. Rather, these qualifying taxpayers either can treat inventories as nonincidental materials and supplies or move to a method that conforms to its applicable financial statement method. Taxpayers qualifying under the $25 million gross receipts test are also excluded from the uniform capitalization rules of section 263A.

The Act also expands the exception for small construction contracts from using the percentage-of-completion method under section 460 for contracts that are expected to be completed within two years of commencement of the contract, and that are performed by a taxpayer that meets the $25 million gross receipts test.

Research and experimental expenditures: Beginning in 2022, the Act requires research and experimental expenditures to be capitalized and amortized ratably over a five-year period. Any such expenditures attributable to research conducted outside the United States must be capitalized and amortized over a 15-year period. These rules do not apply to expenditures for the acquisition or improvement of land, or for expenditures paid to ascertain the existence, location, extent, or quality of mineral deposits, including oil and gas. Software development expenditures shall be treated as research or experimental expenditures.

Sexual harassment or sexual abuse payments: The Act denies a deduction for payments related to sexual harassment or sexual abuse, where the payment is subject to a nondisclosure agreement. Additionally, attorney's fees related to such settlement or payment may not be deducted. This rule applies to payments made after the date of enactment.

Fines and penalties: The Act denies a deduction for any amounts paid or incurred to, or at the direction of, a government or governmental entity in relation to the violation of any law or investigation into the potential violation of any law. This provision thus increases the scope of nondeductible fines and penalties under section 162(f). Restitution payments are, however, excluded from this limitation, and can be deducted. The Act also adds the reporting requirement that an appropriate official of the government or governmental entity provide the IRS and each party to the settlement information detailing the amount and nature of any payments and agreement. The provision applies to any amounts paid or incurred on or after the date of enactment.

Interest capitalization for beer, wine, and distilled spirits: Producers must capitalize interest associated with property with a production period exceeding two years, or an estimated production period exceeding one year and costing more than $1 million. Under current law, the production period includes the aging period of goods. However, the Act excludes the aging period for beer, wine, and distilled spirits from the production period for purposes of the UNICAP interest capitalization rules. Therefore, many of these goods may now be excluded from having to capitalize interest.

Business credits

"Orphan drug" credit: The Act modifies the orphan drug credit, a tax credit for clinical testing expenses incurred in the testing of certain drugs to treat rare diseases or conditions, by reducing the credit rate under section 45C to 25 percent of qualified clinical testing expenses (from 50 percent).

Rehabilitation credit: The Act modifies the rehabilitation credit under section 47 for the restoration of old and historic buildings. Prior law provided a 20 percent credit for qualified rehabilitation expenditures with respect to a certified historic structure, and a 10 percent credit for qualified rehabilitation expenditures with respect to a qualified rehabilitated pre-1936 building.

The Act repeals the 10 percent credit for pre-1936 buildings and modifies the 20 percent credit for certified historic structures, generally for amounts paid or incurred after 2017. The credit amount for certified historic structures remains at 20 percent, but is claimed ratably over a five-year period beginning in the tax year in which a qualified structure is placed in service. The Act includes a transition rule under the effective date relating to qualified rehabilitation expenditures under certain phased rehabilitations for which the taxpayer may select a 60-month period. The provision applies to amounts paid or incurred after December 31, 2017. A transition rule provides that in the case of qualified rehabilitation expenditures (for either a certified historic structure or a pre-1936 building), with respect to any building owned or leased (as provided under present law) by the taxpayer at all times on and after January 1, 2018, the 24-month period selected by the taxpayer (section 47(c)(1)(C)(i)), or the 60-month period selected by the taxpayer under the rule for phased rehabilitation (section 47(c)(1)(C)(ii)), is to begin not later than the end of the 180-day period beginning on the Act's enactment date, and the amendments made by the provision apply to such expenditures paid or incurred after the end of the taxable year in which such 24-month or 60-month period ends.

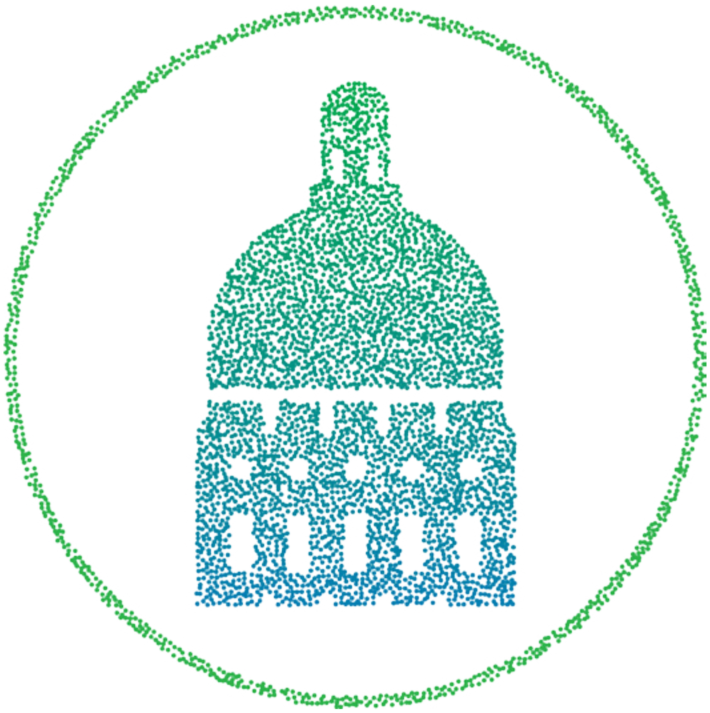
Credit for paid family and medical leave: The Act creates a new employer credit for paid family and medical leave in section 45S that permits eligible employers (employers that allow all qualifying full-time employees at least two weeks of annual paid family and medical leave and allow part-time employees a commensurate amount of leave on a pro rata basis) to claim a business credit for 12.5 percent of the wages paid to qualifying employees during any period in which such employees are on family and medical leave if the payment rate under the program is 50 percent of the wages normally paid to an employee. The credit is increased by 0.25 percentage points (but not above 25 percent) for each percentage point by which the rate of payment exceeds 50 percent.

The credit is effective for wages paid in tax years beginning after December 31, 2017, but does not apply to wages paid in tax years beginning after December 31, 2019.

Other general business credits: Notably, the Act generally retains other general business credits, including the research credit, low-income housing tax credit, new markets tax credit, work opportunity tax credit, FICA tip credit, employer provided childcare credit, access to disabled individuals credit, production tax credit, energy investment tax credit, plug-in electric vehicle credit, enhanced oil recovery credit, marginal well credit, and nuclear production tax credit. Further, it leaves in place the deduction for certain unused business credits under section 196.

Base Erosion and Anti-Abuse Tax: It is noteworthy that certain multinational companies claiming any general business credits could be impacted by the Base Erosion and Anti-Abuse Tax (BEAT) in section 59A. The Act creates the BEAT, which provides a base erosion minimum tax of 5 percent in 2018, 10 percent in 2019 through 2025 (11 percent for banks and securities dealers), and 12.5 percent after 2025 (13.5 for banks and securities dealers). The Act provides that certain general business credits may be claimed against BEAT liability through 2025 (research credits and 80 percent of low-income housing tax credits, investment tax credits, and production tax credits).

The BEAT provision may have a significant impact on the ability of major financial institutions to participate in the tax equity financing marketplace. The BEAT would be applicable to credits generated as a result of projects that began operating in prior years. (See additional discussion on the BEAT in the international tax section of this publication.)



Pass-through provisions

The Act introduces new rules aimed at providing greater parity between the tax treatment of owners of pass-through entities and corporations, but also includes guardrails intended to prevent pass-through owners from recharacterizing wage income as more lightly taxed business income.

20 percent deduction of domestic qualified business income

Under the Act, an individual, estate, or trust taxpayer generally may deduct the sum of:

- Twenty percent of the domestic qualified business income with respect to a qualified trade or business from a partnership, S corporation, or sole proprietorship (subject to certain limitations based on W-2 wages and capital and, with respect to specified service businesses, only below certain taxpayer income thresholds), and
- Twenty percent of aggregate qualified real estate investment trust (REIT) dividends, qualified cooperative dividends, and qualified publicly traded partnership income.

Qualified business income for a taxable year means the net amount of domestic qualified items of income, gain, deduction, and loss with respect to the taxpayer's qualified trades or businesses (that is, any trade or business other than specified service trades or businesses, defined below).

Qualified business income does not include any amount paid by an S corporation that is treated as reasonable compensation of the taxpayer. Similarly, qualified business income does not (to the extent provided in regulations) include any amount paid by a partnership to a partner who is acting other than in his or her capacity as a partner for services rendered with respect to the trade or business, and does not include any amount that is a guaranteed payment for services actually rendered to or on behalf of a partnership to the extent that the payment is in the nature of remuneration for those services. In addition, qualified business income does not include certain investment-related income, gain, deductions, or loss.

For taxpayers with income lower than a threshold amount ($157,500 for single filers, $315,000 for joint filers, with any potential deduction phased out over the next $50,000 or $100,000 of taxable income, respectively), there is no wage limitation on the 20 percent deduction for qualified business income. (Note that the threshold amount is determined by reference to the taxpayer's taxable income, which may include income from other sources.) These taxpayers also are not subject to the limitation on specified service businesses described below.

For taxpayers with income above a threshold amount, a limitation on the 20 percent deduction applies. With respect to each qualified trade or business, the amount of the deduction is limited to the greater of (1) 50 percent of the W-2 wages with respect to the qualified trade or business, or (2) 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.

Qualified property means: (1) 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, (2) which is used in the production of qualified business income, and (3) for which the depreciable period has not ended before the close of the taxable year. 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 (1) the date 10 years after that date, or (2) 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)).

As mentioned above, a specified service business is not a qualified trade or business. A "specified service business" means any trade or business involving the performance of services in the fields of health, law, 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.) A specified service business, however, does not include a trade or business involving engineering or architecture.

In the case of a partnership or S corporation, the provision applies at the partner or shareholder level, as the case may be. Each partner takes into account the partner's allocable share of each qualified item of income, gain, deduction, and loss, and is treated as having W-2 wages for the taxable year equal to the partner's allocable share of W-2 wages of the partnership. 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. Similarly, each shareholder of an S corporation takes into account the shareholder's pro rata share of each qualified item of income, gain, deduction, and loss, and is treated as having W-2 wages for the taxable year equal to the shareholder's pro rata share of W-2 wages of the S corporation. A partner's allocable share or an S corporation shareholder's pro rata share of the unadjusted basis of a partnership's or S corporation's qualified property is determined in the same manner as the partner's or shareholder's allocable or pro rata share of depreciation from the partnership or S corporation.

In addition to a 20 percent deduction for a taxpayer's qualified business income, a 20 percent deduction is also available for (1) dividends from a REIT (other than any portion that is a capital gain dividend) and (2) qualified publicly traded partnership (PTP) income (generally including domestic business income allocated from a PTP and excluding investment related items from PTPs).

With respect to trusts and estates, rules similar to the rules under prior-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.

The Secretary of the Treasury is required to provide rules for applying the limitation in cases of a short taxable year or 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. The Secretary is required to provide guidance applying rules similar to the rules of section 179(d)(2) to address acquisitions of property from a related party, as well as in a sale-leaseback 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, the Secretary is required to provide guidance prescribing rules for determining the unadjusted basis immediately after acquisition of qualified property acquired in like-kind exchanges or involuntary conversions, and guidance for the application of the provision in the case of tiered entities.

The provision applies to taxable years beginning after December 31, 2017, and expires for taxable years beginning after December 31, 2025.

Accuracy-related penalty applies to the 20 percent deduction: Section 6662(d) imposes an accuracy-related penalty on taxpayers with a substantial understatement of tax. The Act provides that for a taxpayer claiming the pass-through business deduction, there is a substantial understatement of income tax for any taxable year if the understatement for the year exceeds $5,000 or 5 percent of the tax required to be shown on the return, rather than the usual 10 percent. This provision is effective for tax years beginning after December 31, 2017.

Repeal of technical termination of partnerships

Under prior law, a partnership terminated if within a 12-month period there was a sale or exchange of 50 percent or more of the total interests in partnership capital and profits (commonly referred to as a "technical termination"). When a technical termination occurred, the business of the partnership continued in the same legal form, but the partnership was treated as newly formed and, thus, among other things, was required to make new elections for various accounting methods and restart depreciation lives.

The Act repeals the technical termination rule. Thus, a partnership is treated as continuing even if 50 percent or more of the total capital and profits interests of the partnership are sold or exchanged, and new elections are not be required or permitted.

The provision applies to partnership taxable years beginning after December 31, 2017.

Recharacterization of certain gains in the case of partnership profits interests held in connection with performance of investment services

The provision treats as short-term capital gain taxed at ordinary income rates the excess of (1) the taxpayer's net long-term capital gain with respect to an applicable partnership interest (API) for the taxable year over (2) the amount of net long-term capital gain with respect to the API for the taxable year calculated as if a three-year (not one-year) holding period applies under section 1222. In making this calculation, the provision calculates long-term capital losses as if a three-year holding period applies.

An API is any interest in a partnership that, directly or indirectly, is transferred to (or held by) the taxpayer in connection with performance of 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. It is intended that partnership interests will 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. An API 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.

An API does not include an interest in a partnership directly or indirectly held by a corporation.

An applicable trade or business means any activity (regardless of whether the activity is 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.

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 to the extent of the partnership's proportionate interest in the foregoing. 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 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.

A special rule provides that, as provided in regulations or other guidance issued by the Secretary, this 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. 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, 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). 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.

The three-year holding period requirement also 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 API, or that an individual may have made a section 83(b) election with respect to an API, does not change the three-year holding period requirement for long-term capital gain treatment with respect to the API.

If a taxpayer transfers any API, directly or indirectly, to a person related to the taxpayer, then the taxpayer includes in gross 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. 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).

The Secretary is directed to require reporting (at the time and in the manner determined by the Secretary) necessary to carry out the purposes of the provision. The Treasury Department also 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. Guidance is also to provide for the application of the provision in the case of tiered structures of entities.

The provision applies to taxable years beginning after December 31, 2017.

Tax gain on the sale of a partnership interest on lookthrough basis

Under Rev. Rul. 91-32, 1991-1 C.B. 107, 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 US 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 US 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 US 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 US trade or business is foreign-source (*Grecian Magnesite Mining v. Commissioner,* 149 T.C. No. 3 (July 13, 2017)).

Under the Act, gain or loss from the sale or exchange of a partnership interest is effectively connected with a US 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. The provision requires that any gain or loss from the hypothetical asset sale by the partnership be allocated to interests in the partnership in the same manner as non-separately stated income and loss.

The provision also requires the transferee of a partnership interest to withhold 10 percent of the amount realized on the sale or exchange of a partnership interest unless the transferor certifies that the transferor is not a nonresident alien individual or foreign corporation. 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.

The provision requires Treasury and the IRS to issue regulations as the Secretary determines appropriate to address coordination with the nonrecognition provisions of the code, including in exchanges described in sections 332, 351, 354, 355, 356, or 361.

Additionally, the conference committee report indicates that the conferees intended that under regulatory authority provided by the Senate amendment to carry out withholding requirements of the provision, the Secretary may 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.

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; 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.

Modification of the definition of substantial built-in loss in the case of transfer of partnership interest

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. Before the Act took effect, section 743(d) provided that 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.

The Act 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 prior-law definition, a substantial built-in loss also exists if the transferee would be allocated a net loss in excess of $250,000 upon a hypothetical disposition by the partnership of all partnership assets in a fully taxable transaction for cash equal to the assets' fair market values, immediately after the transfer of the partnership interest. Therefore, the test for a substantial built-in loss under the provision applies both at the partnership level and at the transferee partner level.

The provision applies to transfers of partnership interests after December 31, 2017.

Charitable contributions and foreign taxes taken into account in determining limitation on allowance of partner's share of loss

Under section 704(d), 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). 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 Act modifies the basis limitation on partner losses to provide that the basis limitation on partner losses applies to a partner's distributive share of partnership charitable contributions (as defined in section 170(c)) and foreign taxes (described in section 901). 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.

The provision applies to partnership taxable years beginning after December 31, 2017.

Loss limitation rules applicable to individuals

Under prior law, a limitation on excess farm losses applied to taxpayers other than C corporations. If a taxpayer other than a C corporation received an applicable subsidy for the taxable year, the amount of the excess farm loss was not allowed for the taxable year, and was carried forward and treated as a deduction attributable to farming businesses in the next taxable year.

The Act expands the limitation on excess farm losses to apply to excess business losses of a taxpayer. Under the provision, excess business losses of a taxpayer other than a C corporation are not allowed for the taxable year. Such losses are carried forward and treated as part of the taxpayer's NOL carryforward in subsequent taxable years. NOL carryovers 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.

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, over the sum of aggregate gross income or gain of the taxpayer plus a threshold amount. The threshold amount for a taxable year is $500,000 for married individuals filing jointly and $250,000 for other individuals. The $500,000 and $250,000 thresholds are indexed for inflation.

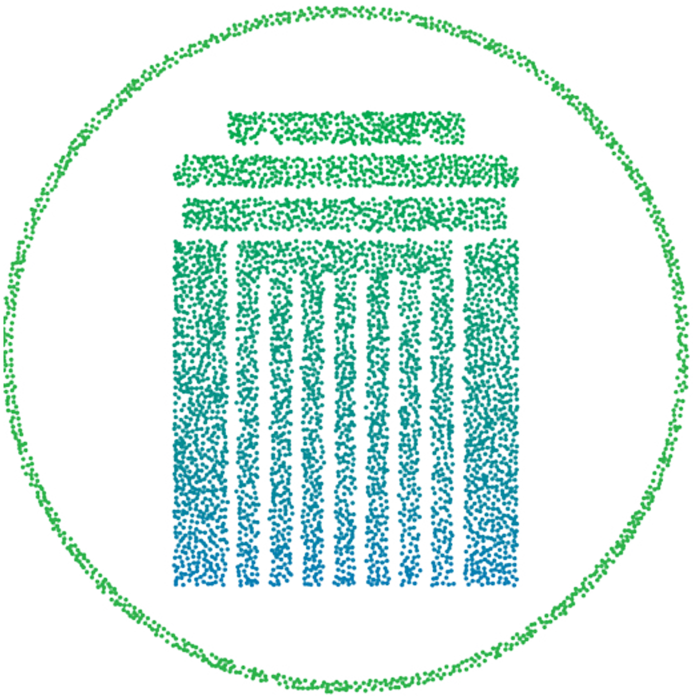
In the case of a partnership or S corporation, the provision applies at the partner or shareholder level. Each partner's or S corporation shareholder's share of items of income, gain, deduction, or loss of the partnership or S corporation are taken into account in applying the limitation under the provision for the taxable year of the partner or S corporation.

The provision is effective for taxable years beginning after December 31, 2017, and before January 1, 2026.

Special subchapter S provisions

For subchapter S corporations, the Act includes provisions related to electing small business trusts, special rules for conversions to C-corporation status, and a deferral election for S corporation shareholders for recognition of accumulated foreign income.

- **ESBTs:** The Act expands the qualifying beneficiaries of an electing small business trust to include nonresident aliens. It also amends the ESBT S-portion charitable deduction rules to provide that the charitable contribution deduction of an ESBT is not determined by the rules generally applicable to trusts but rather by the rules applicable to individuals. 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. The provision applies to taxable years beginning after December 31, 2017.
- **Special rules on conversion of S corporations to C corporations:** 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. An eligible terminated S corporation is any C corporation which: (1) is an S corporation the day before the enactment of the Act; (2) during the two-year period beginning on the date of such enactment revokes its S corporation election under section 1362(a); 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. Under the provision, in the case of a distribution of money by an eligible terminated S corporation, the accumulated adjustments account 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. Any increase in tax due to the section 481(a) adjustment, rather than the section 481(a) adjustment itself, is taken into account ratably during the six-taxable-year period beginning with the year of change. The provision is effective for distributions after the date of enactment.
- **Deferral election allowed for S corporation shareholders for recognition of accumulated foreign income:** A special rule permits deferral of the transition net tax liability for shareholders of a US shareholder that is an S corporation. The S corporation is required to report on its income tax return the amount includible in gross income by reason of this provision, as well as the amount of deduction that would be allowable, and provide a copy of such information to its shareholders. Any shareholder of the S corporation may elect to defer his or her 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. 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. (See additional discussion of international tax issues elsewhere in this publication.)



International tax issues

Transition to territoriality

Dividends received deduction: The Act provides for a 100 percent dividends received deduction for the foreign-source portion of dividends received from specified 10-percent-owned foreign corporations by domestic corporations that are US shareholders. For this purpose, an amount received by a domestic corporation that is treated as a dividend under section 1248 is treated as a dividend for purposes of the DRD (provided the holding period requirements are satisfied). In addition, if the gain is recognized by a lower tier CFC and characterized as a dividend under section 964(e), then such amount is included in subpart F income for the year of the sale but the US shareholder can claim a DRD with respect to such amount.

No foreign tax credit or deduction is allowed for taxes paid or accrued with respect to such dividend that qualifies for the DRD.

In addition, consistent with the Senate legislation, the bill provides: (1) a limitation on the DRD for any dividend received if the foreign corporation receives a deduction (or other tax benefit) from taxes imposed by a foreign country (hybrid dividend) and (2) an expanded holding period requirement.

Finally, the conference committee explanation provides that any hybrid dividend received by a CFC is treated as subpart F income for the taxable year such dividend was received.

Limitation on losses with respect to 10-percent-owned foreign corporations: The basis in foreign corporations with respect to which the dividends received deduction applies is reduced by the amount of any such dividend, but only for purposes of computing loss on the sale or exchange of that stock.

Taxation of deferred foreign income upon transition: Consistent with the House bill and the Senate bill, a US shareholder of a foreign corporation must include in income for the subsidiary's last tax year beginning before January 1, 2018, the shareholder's pro rata share of undistributed and previously untaxed post-1986 foreign earnings. Earnings and profits (E&P) is only taken into account to the extent it was accumulated during periods when the foreign corporation was a CFC or was a non-CFC foreign corporation that had at least one domestic corporation as its US shareholder.

The amount of such E&P is the greater of the amounts determined as of November 2, 2017, or December 31, 2017, unreduced by dividends (other than dividends to other specified foreign corporations) during the taxable year to which the provision applies.

The mandatory inclusion generally may be reduced by foreign earnings and profits deficits (including hovering deficits) that are properly allocable to that person. In addition, unlike the Senate bill, the mandatory inclusion may be reduced by the pro rata share of deficits of another US shareholder that is a member of the same affiliated group.

For purposes of this provision, the E&P is classified as either E&P that has been retained in the form of cash or cash equivalents, or E&P that has been reinvested in the foreign subsidiary's business (for example, property, plant, and equipment). The portion of the E&P comprising cash or cash equivalents is taxed at a reduced rate of 15.5 percent, while any remaining E&P is taxed at a reduced rate of 8 percent.

Rules will be provided to avoid the double counting of cash assets. In addition, the Act grants regulatory authority to the Treasury to issue regulations to prevent the avoidance of the rules, including through a reduction of earnings and profits, through changes in entity classification, or accounting methods, or otherwise.

Limitation on assessment extended: Consistent with the Senate bill, the Act extends the assessment statute of limitations for taxpayers reporting a mandatory inclusion. The assessment statute of limitations is generally extended to six years from the date upon which the return was filed that initially reflects the mandatory inclusion.

Special rules for expatriated entities: Consistent with the Senate bill, the enacted legislation increases the rate of tax imposed on the deferred earnings of a specified foreign corporation if within 10 years of the date of enactment, the US shareholder of such corporation engages in an "inversion transaction" subject to section 7874.

Other provisions: In addition, the legislation provides: (1) that foreign tax credit carryforwards are fully available, and foreign tax credits triggered by the deemed repatriation are partially available, to offset the US tax; (2) that at the election of the US shareholder, the tax liability would be payable over a period of up to eight years; (3) special rules which would apply with respect to S corporations and their shareholders, as well as REITs; and (4) an election not to apply any net operating loss deduction against the amount taken into account under the transition tax rules.

Rules related to passive and mobile income

Global intangible low-taxed income: The enacted legislation largely adopts, with modifications, provisions in the Senate bill designed to tax currently global intangible low-taxed income (GILTI). Under the provision, a US shareholder is required to include in gross income the amount of its GILTI. However, the US shareholder is allowed a deduction equal to 50 percent of the GILTI and the amount treated as a dividend by reason of the US shareholder claiming a foreign tax credit as a result of the inclusion of the GILTI amount in income ("section 78 gross up").

GILTI is the excess of the shareholder's net tested income over the deemed tangible income return, which is defined as the excess of 10 percent of the shareholder's basis in tangible property used to produce tested income less the amount of interest expense allocated to net tested income. The reduction of this amount by allocated interest expense is a change from the original Senate bill and more closely follows an approach adopted by the House Ways and Means Committee with respect to their proposal.

Tested income for this purpose is the gross income of the corporation determined without regard to the following exceptions: (1) the corporation's effectively connected income 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 and foreign oil related income, over deductions (including taxes) properly allocable to such gross income under rules similar to the rules of section 954(b)(5).

Consistent with the Senate bill, the amount of GILTI included by a US shareholder is allocated across all of such shareholder's CFCs, based on each CFC's proportionate share of tested income. In addition, the shareholder can claim a foreign tax credit for 80 percent of the taxes paid or accrued with respect to the tested income of each CFC from which the shareholder has an inclusion.

Deduction for foreign-derived intangible income: In addition to the immediate inclusion of GILTI, the Act allows a domestic corporation a deduction for 37.5 percent of the foreign-derived intangible income and a 50 percent deduction of the GILTI plus the section 78 gross up, as discussed above. These deductions are reduced to 21.875 percent and 37.5 percent, respectively, in taxable years beginning after December 31, 2025.

Foreign-derived intangible income is an amount equal to the corporation's deemed intangible income multiplied by an amount equal to the corporation's foreign-derived, deduction-eligible income over its total deduction-eligible income.

Deduction-eligible income is the gross income of the corporation determined without regard to: (1) the subpart F income of the corporation under section 951; (2) the GILTI of the corporation; (3) financial services income; (4) any dividend received from a CFC with respect to which the corporation is a US shareholder; (5) any domestic oil and gas income of the corporation; and (6) any foreign branch income (as defined in section 904(d)(2)(J)) of the corporation, over the deductions (including taxes) properly allocable to such gross income.

Deemed intangible income is the excess of a corporation's deduction-eligible income over 10 percent of the basis in its tangible depreciable property used to produce deduction-eligible income.

Foreign-derived, deduction-eligible income means with respect to a taxpayer for its taxable year, 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 US 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. For this purpose, the terms sold, sells, and sale include any lease, license, exchange, or other disposition of property.

Unlike the Senate bill, the Act does not provide a rule presumably intended to incentivize the onshoring of intangible property, by providing that if a CFC holds intangible property on the date of enactment, the fair market value of the property on the date of any distribution is treated as not exceeding its adjusted basis.

Treatment of hybrid transactions

The Act includes the provision from the Senate bill that would deny the deduction for any disqualified related-party amount paid pursuant to a hybrid transaction or by or to a hybrid payment. A disqualified related-party amount is any interest or royalty paid or accrued to a related party to the extent that: (1) there is no corresponding inclusion to the related party under the tax law of the country of which such related party is a resident for tax purposes, or (2) such related party is allowed a deduction with respect to such amount under the tax law of such country.

A hybrid transaction is any transaction, series of transactions, agreement, or instrument one or more payments with respect to which are treated as interest or royalties for federal income tax purposes and which are not so treated for purposes of the tax law of the foreign country of which the recipient of such payment is resident for tax purposes or is subject to tax.

A hybrid entity is any entity which is either: (1) treated as fiscally transparent for federal income tax purposes but not so treated for purposes of the tax law of the foreign country of which the entity is resident for tax purposes or is subject to tax, or (2) treated as fiscally transparent for purposes of the tax law of the foreign country of which the entity is resident for tax purposes or is subject to tax but not so treated for federal income tax purposes.

Base erosion proposals

The Act adopts the Senate bill's provisions related to base eroding payments, with certain modifications. Accordingly, a corporation (other than a RIC, REIT or S corporation) with excess base erosion payments for the taxable year must pay a tax equal to the excess of 10 percent (5 percent for taxable years beginning in 2018) of its taxable income (determined without regard to deductions attributable to base erosion payments) over its regular tax liability reduced by the excess of credits allowed under Chapter 1 against the regular tax liability over the sum of the R&D credit plus 80 percent of the sum of the low-income housing credit, the renewable electricity production credit determined under section 45(a), and the energy property investment credit determined under section 48.

For purposes of this provision, a base erosion payment generally 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, including 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 also includes any amount that constitutes reductions in gross receipts of the taxpayer that is paid to 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 became a surrogate foreign corporation after November 9, 2017, and (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).

A base erosion payment does not include: (1) any amount paid or accrued for services if such services meet the requirements for eligibility of the services cost method in Treas. Reg. sec. 1.482-9, without regard to certain requirements of that section and provided the payments are made without a mark-up, and (2) a "qualified derivative payment." In addition, a corporation is not subject to the provision if it has average annual gross receipts for the three-taxable-year period ending with the preceding taxable year of less than $500 million or its base erosion percentage is less than 3 percent. (The term base erosion percentage means for any taxable year, the percentage determined by dividing the aggregate amount of deductions attributable to base eroding payments by the total amount of all deductions allowable to the taxpayer during the taxable year, without regard to deductions under sections 172, 245A or 250, any deduction for services which are not treated as base eroding payments, and any deduction for qualified derivative payments. In the case of a bank or registered securities dealer, the 3 percent base erosion percentage threshold is lowered to 2 percent.)

Information reporting requirement: The Act provides for increased information reporting under sections 6038A and 6038C to require certain taxpayers subject to the new base erosion provisions to report information such as base erosion payments, information for determining the base erosion minimum tax, and other information deemed necessary by the Secretary of the Treasury. In addition, it increases the penalty from $10,000 to $25,000 for failure to comply with section 6038A and increases the penalty for failure to comply within 90 days after IRS notification to $25,000 for each 30-day period thereafter.

Interest expense limitation

Section 163(j): The general limitation on interest deductibility contained in section 163(j) is modified and generally follows the proposal included in the Senate bill. Details on this provision are included in the discussion of corporate tax issues elsewhere in this report.

Section 163(n): The provisions that were originally included in both the House and Senate bills addressing interest expense incurred by domestic corporations that are members of an international group were not included in the enacted legislation.

Other international provisions

Codification of Rev Rul. 91-32: The bill adopts the Senate proposal with respect to Rev. Rul. 91-32. Accordingly, gain or loss from the sale or exchange of a partnership interest is effectively connected with a US 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. The Act requires that any gain or loss from the hypothetical asset sale by the partnership be allocated. In addition, the transferee of a partnership interest is required to withhold 10 percent of the amount realized on the sale or exchange of a partnership interest unless the transferor certifies that the transferor is not a nonresident alien individual or foreign corporation.

Although the provision applies to sales or exchanges on or after November 27, 2017, the portion imposing the withholding tax obligation applies to sales or exchanges occurring after December 31, 2017. The Treasury Department and IRS, however, announced in Notice 2018-08 (released December 29, 2017) that withholding is suspended pending the issuance of further guidance.

In addition, the Act includes provisions to:

- Modify the definition of a US shareholder to include any US person who owns 10 percent or more of the total value of the foreign corporation (as opposed to vote);
- Modify the definition of section 936(h)(3)(B) to include workforce in place, goodwill, and going concern value;
- Impose a limitation on claiming lower rates on dividends from certain corporations subject to section 7874;
- Impose a separate foreign tax credit limitation category for branch income;
- Repeal the fair market value method for allocating interest expense;
- Eliminate foreign base company oil-related income as a category of subpart F income;
- Provide for an inflation adjustment to the de minimis rule;
- Repeal subpart F inclusions based on the withdrawal of previously excluded subpart F income invested in foreign base company shipping operations;
- Eliminate the limitation on attribution of stock from a foreign person to a US shareholder;
- Eliminate the requirement that a foreign corporation must be a CFC for an uninterrupted period of 30 days for subpart F to apply;
- Repeal the section 902 credit and application of the section 960 credit on a current-year basis; and
- Change the source rules for the sale of inventory property.

Finally, and unlike the prior versions of the bill, the Act does not repeal section 956, does not make permanent section 954(c)(6), and does not accelerate the election to allocate interest expense on a worldwide basis.

Insurance provisions

The Act includes 13 provisions that change the taxation of US insurance companies and products.

- Five of these provisions were included in both the House and Senate bills: change in operating loss carrybacks and carryforwards for life insurers, small life company deduction repeal, change in basis (section 807(f)) revisions, repeal of section 815, and repeal of section 847.
- The provisions addressing life reserves, life company proration, and deferred acquisition costs (DAC, section 848) as well as the three life product-related provisions, were not included in the House bill as passed but were included in the Senate bill.
- The 8 percent surtax "placeholder" that passed the House is eliminated.
- A few of the proposals would appear to simplify the insurance provisions of the code.

General corporate NOL carryback and carryover periods apply to life insurers

The Act adopts substantially similar provisions in the House and Senate bills that put life insurance companies on the general section 172 net operating loss rules for operations loss carrybacks (zero years) and operations loss carryovers (indefinite). Under the revised NOL rules in section 172, the use of net operating losses from previous years will be allowed to offset up to 80 percent of current-year taxable income.

The general corporate loss carryover and carryback regime apply to losses of life insurers arising in taxable years beginning after December 31, 2017, that is, for losses arising in 2018 and thereafter for calendar-year taxpayers.

The Act retains the special 2-year back, 20-year forward carryback and carryover rule for nonlife insurance companies by amending section 172, and exempts nonlife insurance companies from the 80 percent limitation on use of NOLs described above.

Repeal of small life insurance company deduction

The Act repeals the small life insurance company deduction (prior-law section 806) and makes corresponding revisions to sections 453B(e) and 953(b) as well. The small life deduction will no longer be available starting in taxable years beginning after December 31, 2017.

Repeal of change in basis 10-year-spread

The Act treats a change in a taxpayer's basis of computing reserves under the regular change in method of accounting rules with a section 481 adjustment rather than allowing a 10-year spread of the difference between year-end reserves under the old and new basis of computing reserves. The section 481 treatment will result in the recognition of an increase in reserves in the year of change and the spreading of a decrease in reserves over four years. The change will be treated as initiated by the taxpayer and made with the consent of the Secretary of the Treasury.

This provision is effective for taxable years beginning after December 31, 2017. Presumably there will be no change in existing spreads for current 807(f) amounts; however, this is not addressed in the legislative text or the description of the provision in the conference report.

Repeal of special rule for distributions from policyholders surplus accounts

The Act repeals section 815, which prescribes rules regarding taxation of certain distributions from policyholders surplus accounts (PSAs). This provision is a remnant from the pre-1984 Act three-phase system of taxation of life insurers under the Life Insurance Company Tax Act of 1959. Any remaining balance of the policyholders surplus account will be included in income over eight years beginning in 2018.

Modification of proration rules for property-casualty insurance companies

The Act increases the proration percentage for property and casualty companies in section 832(b)(5) to 5.25 percent divided by the highest corporate tax rate, i.e., the proration percentage will jump from 15 percent to 25 percent for the 2018 taxable year.

This provision is effective for taxable years beginning after December 31, 2017.

Repeal of special estimated tax payments

The Act repeals section 847, which provides for special estimated tax payments.

This provision is effective for taxable years beginning after December 31, 2017. Any special loss account balances will be included in taxable income for the 2018 taxable year. Any excess tax payments will be treated as payments under section 6655.

Life insurance reserves are based on statutory reserves with 'haircut'

The Act adopts, with modifications, a Senate proposal that eliminates the federally prescribed reserve (FPR) computation for life insurance reserves and instead bases tax reserves on the greater of the net surrender value of a contract and 92.81 percent of statutory reserves.

Life insurers are required to report the opening balance and closing balance of reserves with respect to the method of computing reserves for purposes of determining income. Details of the method for reporting reserves are not specified.

The revised reserve computation is effective for taxable years beginning after December 31, 2017. A transition rule allows any difference between the prior year-end reserves computed on the old basis and on the new basis to be spread over eight years as either income or a deduction.

The House bill as passed did not include a life reserves change and instead included the 8 percent surtax on life companies.

Modification of life company DRD proration rules

The Act adopts a Senate proposal that modifies the life company proration rules by defining the section 812 “company’s share” as 70 percent, and defining the “policyholders’ share” as 30 percent for purposes of the dividends received deduction and tax-exempt interest income.

This provision is effective for taxable years beginning after December 31, 2017.

The House bill as passed did not include a proration change and instead included an 8 percent surtax on the taxable income of life companies.

Increase DAC capitalization rates

The Act increases capitalization rates for determining “specified policy acquisition expenses” and extends the amortization period for capitalized DAC amounts. The provision increases the capitalization rate for annuity contracts from 1.75 percent to 2.09 percent, the rate for group life insurance contracts from 2.05 percent to 2.45 percent, and the rate for all other specified insurance contracts from 7.7 percent to 9.2 percent.

The amortization period for capitalized DAC amounts is extended to 180 months (from 120 months).

This provision is effective for taxable years beginning after December 31, 2017. A transition rule allows capitalized DAC amounts as of December 31, 2017 to continue under 10-year amortization.

The House bill as passed did not include a DAC change and instead included an 8 percent surtax on life companies.

Modification of discounting rules for property-casualty insurance companies

The Act modifies (generally, increases) the discount rate applied to compute unpaid loss reserves of property and casualty insurers under section 846. The rate is modified from the 60-month rolling average of the applicable federal mid-term interest rate (AFR) to a rate based on the corporate bond yield curve for the preceding 60-month period on investment grade corporate bonds with varying maturities and that are in the top three quality levels available.

The provision also changes applicable loss payment patterns for long tail lines of business to extend a maximum of 24 years, rather than 15 years.

The proposal also repeals the section 846(e) election which allowed an insurer to use its own historical payment patterns for discounting unpaid losses.

This provision is effective for taxable years beginning after December 31, 2017. Under a transition rule for the first taxable year beginning in 2018, the amount of unpaid losses and expenses at the end of the preceding taxable year (2017) is determined as if the provision had applied to these items in such preceding taxable year. Any adjustment will be spread over eight taxable years beginning in 2018.

Tax reporting requirement for life settlement transactions

The Act adds section 6050Y and imposes a tax reporting requirement on the purchaser for certain acquisitions of existing life insurance contracts (i.e., "reportable policy sales") and on the insurance company upon payment of death benefits in certain situations (i.e., "reportable death benefits").

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 is treated as a reportable policy sale. In the event of such sale, the buyer is required to report information about the purchase to the IRS, to the insurance company that issued the contract, and to the seller. Upon payment of death benefit proceeds, reporting is required by the insurance company that issued the relevant contract.

The reporting requirement is effective for reportable policy sales occurring after December 31, 2017, and reportable death benefits paid after December 31, 2017.

Clarify tax basis of life insurance contracts

The Act provides that the owner of an annuity or life insurance contract determines basis in the contract without reduction for the cost of insurance or mortality charges. This provision overrides the IRS's recent position on reduction of basis for purposes of determining gain or loss on the disposition of a life or annuity contract.

The clarification of the basis rules for life insurance and annuity contracts is effective retroactively to 2009 for transactions entered into after August 25, 2009.

Narrow the exception to transfer for value rules

The Act narrows the exceptions to the transfer for value rules in section 101(a)(2) in the case of a transfer of a life insurance contract, or any interest in a life insurance contract, in a reportable policy sale that would be the subject of the new information reporting rule in section 6050Y.

The provision is effective for transfers occurring after December 31, 2017.

Restrict insurance business exception to passive foreign investment company rules

The Act amends the active insurance exception in the passive foreign investment company (PFIC) rules to add subsection (f) to section 1297 and provide that the exception will be generally available only to a foreign corporation that would be taxed as an insurance company if it were a domestic corporation and if its loss and loss adjustment expenses and reserves (other than deficiency, contingency, or unearned premium reserves) for life and health insurance risks and life and health insurance claims with respect to contracts providing coverage for mortality or morbidity risks constitute more than 25 percent of the foreign corporation's total assets.

The amendment to the active insurance exception to the PFIC rules is effective for taxable years beginning after 2017.

Tax provisions affecting individuals

The individual tax provisions in the Act generally track with those in the Senate-approved bill—including, most significantly, the fact that nearly all of the changes to the individual side of the code expire after 2025.

Tax rate modifications

Consistent with the Senate proposal, the Act maintains seven brackets as in prior law while reducing the highest tax bracket from the prior-law level of 39.6 percent to 37 percent for single filers with taxable income over $500,000. (The Senate-approved version provided for a top rate of 38.5 percent.)

Notably, the threshold for the 37 percent bracket for married filing joint taxpayers is only $600,000, and as a result these new rate tables re-establish the so-called "marriage penalty." Also worth noting is the fact that the enacted legislation does not incorporate the "bubble tax" proposed in the House bill, which would have erased the benefits of the lowest tax bracket for high-income taxpayers.

As with both the House and Senate proposals, the Act retains the 20 percent special tax rate for long-term capital gains and qualified dividend income, the 3.8 percent tax rate on certain levels of net investment income, and the 0.9 percent FICA-HI tax rate on certain levels of earned income that were in effect under prior law.

Ordinary income tax rates compared: Tax reform legislation as enacted vs. 2017 law											
2017 law (tax year 2018)						Tax reform legislation as enacted (tax years 2018-2025)					
Single			Married couples filing joint			Single			Married couples filing joint		
Ordinary Income	Taxable income over	But not more than	Ordinary Income	Taxable income over	But not more than	Ordinary Income	Taxable income over*	But not more than	Ordinary Income	Taxable income over*	But not more than
10%	-	$9,525	10%	-	$19,050	10%	-	$9,525	10%	-	$19,050
15%	$9,525	$38,700	15%	$19,050	$77,400	12%	$9,525	$38,700	12%	$19,050	$77,400
25%	$38,700	$93,700	25%	$77,400	$156,150	22%	$38,700	$82,500	22%	$77,400	$165,000
28%	$93,700	$195,450	28%	$156,150	$237,950	24%	$82,500	$157,500	24%	$165,000	$315,000
33%	$195,450	$424,950	33%	$237,950	$424,950	32%	$157,500	$200,000	32%	$315,000	$400,000
35%	$424,950	$426,700	35%	$424,950	$480,050	35%	$200,000	$500,000	35%	$400,000	$600,000
39.6%	$426,700		39.6%	$480,050		37%	$500,000		37%	$600,000	

* Under the Act, the income thresholds for the individual rate brackets will be adjusted for inflation using the Chained Consumer Price Index for All Urban Consumers. This is a permanent change.

The table above illustrates how the tax rates under the Act compare to prior law.

Individual alternative minimum tax

While the proposals that were approved in the House and the Senate would have repealed the alternative minimum tax, the Act maintains the AMT for individual and fiduciary income taxpayers, albeit with a higher exemption amount of $70,300 for single taxpayers and $109,400 for married taxpayers filing a joint return. Further, the phaseout thresholds are increased to $500,000 and $1 million for single and joint filers, respectively. Both the exemption and phaseout threshold amounts are indexed for inflation.

Pass-through taxation on individual returns

For individuals and fiduciaries, the Act includes a 20 percent deduction against "domestic qualified business income" from a partnership, S corporation, or sole proprietorship. (Details on the deduction and on a provision related to excess business losses of individuals are discussed at length in the pass-through business section in this publication.)

Itemized deductions

Consistent with the House and Senate versions, the enacted bill substantially increases the standard deduction to $12,000 for single taxpayers and $24,000 for married taxpayers filing jointly. Additionally, it maintains the prior-law additional standard deduction for the blind and elderly. Increased standard deductions will allow many individuals to avoid itemizing their deductions. However, for those individuals who will still itemize, the enacted bill differs from prior law in several notable respects:

- **Mortgage interest deduction reduced:** The mortgage interest deduction will be limited to interest on $750,000 ($375,000 for married filing separate taxpayers) of acquisition indebtedness on a taxpayer's primary and secondary residences. Mortgages existing on or before December 15, 2017 (and certain others where there is a binding contract to purchase property before December 15, 2017 or are refinanced) are grandfathered under the prior-law $1 million threshold. The interest deduction for home equity indebtedness is repealed.

- **Medical and dental expense deduction expanded:** Unreimbursed medical and dental expenses will be deductible to the extent they exceed 7.5 percent of adjusted gross income (AGI) in 2017 and 2018. The percentage increases to 10 percent (the threshold in effect under pre-enactment law) in 2019. The threshold applies to both the regular and alternative minimum tax.
- **Miscellaneous itemized deductions eliminated:** The Act eliminates all miscellaneous itemized deductions that are not listed in section 67(b). For fiduciary taxpayers, the statutory wording of new section 67(g) appears to preclude a deduction for any administrative cost (e.g., trustee fees, investment management and custodial fees, and attorney/accounting fees). Further guidance will be required.
- **Personal casualty losses limited:** The Act provides that personal casualty losses are deductible pursuant to other current-law rules only if the losses were incurred in federally declared disaster areas.
- **State and local income or sales and property tax deductions limited:** An itemized deduction of up to $10,000 ($5,000 for married taxpayers filing a separate return) for the aggregate of nonbusiness (1) state and local property taxes, and (2) state and local income taxes or sales taxes is permitted. Nonbusiness foreign real property taxes are no longer deductible. It does not appear that the $10,000 limitation is indexed for inflation. Significantly, prepayments of state and local income tax for 2018 made in 2017 are treated as paid as of the last day of 2018, and recent guidance from the IRS indicates that prepayments in 2017 of 2018 property taxes will be deductible only if those taxes were actually assessed in 2017.
- **Charitable contributions modified:** The AGI limit for gifts of cash to public charities and certain other organizations is increased from 50 percent to 60 percent. However, a charitable deduction is now denied for payments made in exchange for college athletic event seating rights.
- **Pease limitation repealed:** The reduction for overall itemized deductions for higher income taxpayers is eliminated.

A table comparing the treatment of itemized deductions under the Act and prior law is available in the appendix at the end of this publication.

Other deductions and exclusions

Consistent with both the House and Senate versions, the enacted bill repeals the deduction for personal exemptions.

It also repeals the moving expense deduction and the exclusion from gross income and wages for qualified moving expense reimbursements, but provides exceptions for active duty members of the armed forces who are moving pursuant to military orders.

Interestingly, though the House and Senate versions of the bill would have modified the exclusion of gain from sale of principal residence provisions to expand the time period for which a taxpayer needed to have resided in the home, the enacted bill contains no such provision. As a result, a taxpayer may continue to exclude up to $250,000 of gain (if single) or $500,000 (married filing jointly) from gross income if the home was used as the taxpayer's principal residence two of the past five years.

The Act generally follows the House provisions with respect to the taxation or deduction of alimony payments. Effective for any divorce or separation instrument executed after December 31, 2018 (or modified after December 31, 2018, to conform with this provision), alimony payments will neither be taxable to the recipient or deductible by the payer.

As expected, the Act continues to allow an exclusion from earned income of contributions to qualified retirement savings vehicles such as 401(k) plans and individual retirement accounts.

Credits: The enacted legislation increases the child tax credit to $2,000 per qualifying child, double the amount under current law; of this amount, $1,400 per qualifying child will be refundable. The credit begins to phase out for married filing joint taxpayers with AGI in excess of $400,000. In addition to the credit for qualifying children, the Act also provides for a $500 nonrefundable credit for qualifying dependents other than children.

Additional family-oriented provisions that were retained from prior law include the dependent care credit, the adoption credit, and the exclusion from gross income of up to $5,000 annually for employer-provided dependent care assistance.

Miscellaneous provisions

Other noteworthy provisions affecting individual taxpayers are described below.

- **Carried interest holding period expanded:** The Act expands the holding period requirement to three years for gains on qualified carried interests to be taxed at preferential long-term capital gains rates. (See related discussion on this issue in the pass-throughs section of this publication.)
- **Cost basis of specified securities remains unchanged:** Whereas the Senate bill contained a provision requiring the cost basis of any security sold to be determined on a first-in first-out basis except to the extent average basis method is allowable (as in the case of a RIC), the enacted bill includes no such provision. Under current law, unless the average basis method is permitted, a taxpayer who sells stock that the taxpayer acquired on different dates or at different prices and who does not adequately identify the lot from which the stock is sold, must treat the stock sold on a first-in first-out basis to determine the basis and holding period. (See related discussion on this issue in the corporate tax section of this publication.)
- **Basis in a life insurance policy modified:** The Act includes a Senate provision that provides that the basis in a life insurance policy or annuity contract on the sale of the cash value of the policy is determined without an adjustment for the cost of insurance (mortality expense under the contract), reversing the IRS position in Rev. Rul. 2009-13. (See the insurance section of this publication for additional discussion.)
- **Section 529 plans expanded:** The Act allows section 529 plan funds to be used in connection with elementary or secondary public, private, or religious school tuition and eligible expenses. However, these distributions are limited to $10,000 per year on a per student basis. (A provision in the House-Senate conference agreement that would have designated home-schooling costs as qualified expenses under this provision was stripped out during Senate floor consideration to comply with Byrd Rule concerns and is not included in the text of the enacted law.)
- **Individual mandate penalty eliminated:** Consistent with the Senate bill, the enacted legislation reduces the penalty to zero for individuals who do not maintain qualifying health insurance coverage under the Patient Protection and Affordable Care Act (the "individual mandate"). The reduced penalty is effective for months beginning after December 31, 2018. Unlike other individual provisions in the bill, this one does not sunset after the end of 2025.
- **Filing requirements adjusted:** The enacted legislation clarifies that an individual is not required to file an income tax return if the individual's gross income for the taxable year does not exceed the applicable standard deduction. Under current law, a return is required to be filed if an individual has income which equals or exceeds the personal exemption amount plus the standard deduction applicable to such individual.

Estate, gift, and generation-skipping transfer tax provisions

The pre-enactment tax regime with respect to the estate, gift, generation-skipping transfer (GST) taxes and the income tax basis adjustment to fair market value at death remain unchanged under the Act except that the applicable exclusion amount (the amount that each citizen is entitled to transfer either during life or, if otherwise unused, at death without incurring a current tax) and the GST tax exemption (the amount that may be transferred to skip-persons outright or in trust without giving rise to a present or future GST tax) is doubled to $11.2 million from its existing $5.6 million for transfers occurring after December 31, 2017.

The exclusion and GST exemption continue to be indexed for inflation. However, beginning January 1, 2026, the exclusion amount and the GST exemption will return to the levels that would have prevailed under pre-enactment law.

Tax-exempt organizations

The Act includes a number of provisions related to the operation of or the treatment of contributions to tax-exempt organizations.

Excise tax on executive compensation of tax-exempt organizations

The Act assesses a 21 percent excise tax on a tax-exempt organization for any covered employee whose compensation is greater than $1 million (plus parachute/severance payments). The excise tax applies to any organization that is tax exempt under section 501(a), farmer organizations, organizations whose income is excluded under section 115 (e.g., governmental hospitals and state colleges and universities), and political organizations under section 527. A "covered employee" is any employee or former employee if the employee is one of the top five highest-compensated employees for the taxable year (note that this appears to be the organization's fiscal year) or was a covered employee in any preceding year beginning after December 31, 2016. Thus, once an individual is considered a covered employee the individual remains a covered employee for the remainder of his or her relationship with the organization.

Compensation means wages not including Roth designated contributions. Deferred compensation is taken into account when taxable pursuant to section 457(f). Notably, compensation for purposes of determining covered employees does not include amounts paid to a licensed professional for the performance of medical or veterinary services (physicians, nurses, and veterinarians). The Act conference report summary clarifies that compensation paid to such professionals in any other capacity (e.g., administrative) is taken into account.

Compensation subject to the excise tax includes compensation for services performed at a related organization. The resultant tax is allocated back to each related organization on a pro rata basis.

Compensation whose deductibility is limited under section 162(m) is not taken into account.

The provision instructs the IRS to write regulations to prevent avoidance of tax through services as a non-employee or through the use of a pass-through or other entity. The excise tax is effective for tax years beginning after December 31, 2017.

Unrelated business income related to the provision of certain fringe benefits

Under the Act, unrelated business income (UBI) is increased for any amounts that would be disallowed under section 274 for qualified transportation fringe benefits, a parking facility used in connection with a qualified transportation fringe benefit, and/or an employer provided on-premises athletic facility. If the costs are allocable to a UBI activity and are disallowed under section 274 then the UBI treatment is not applicable. This treatment is also not applicable if employees are taxed on the benefit.

UBI determined by activity

The Act provides that losses from one unrelated business income activity may not offset income from another. Losses from an activity will carry forward and if appropriate may offset future income from the activity. Net operating loss carryforwards from years beginning before January 1, 2018, will continue to carry forward and will not be affected by this change.

Excise tax on the net investment income of private colleges and universities

The Act proposes a 1.4 percent tax on net investment income of a private college or university. The tax is applicable to institutions that:

- Have at least 500 students at least 50 percent of whom are in the United States (an additional requirement included in the House-Senate conference agreement that these be tuition-paying students was stripped out during Senate floor consideration to comply with Byrd Rule concerns and is not included in the enacted law);
- Is not a state college or university; and
- Whose aggregate fair market value of assets at end of the previous taxable year (other than those used directly in carrying on tax-exempt purpose) is at least $500,000 per student.

The number of students is calculated as the daily average number of full-time students attending the college or university. For purposes of determining net assets per student and net investment income subject to tax, net assets held by related parties, including organizations controlled by the college or university and organizations supporting the college or university, are taken into account. The net investment income will be determined under rules similar to those used by private foundations.

Charitable contribution in return for the right to purchase athletic tickets

The Act repeals section 170(l) and states there is no charitable deduction for contributions required in order to obtain the right to purchase tickets to an athletic event at a college or university.

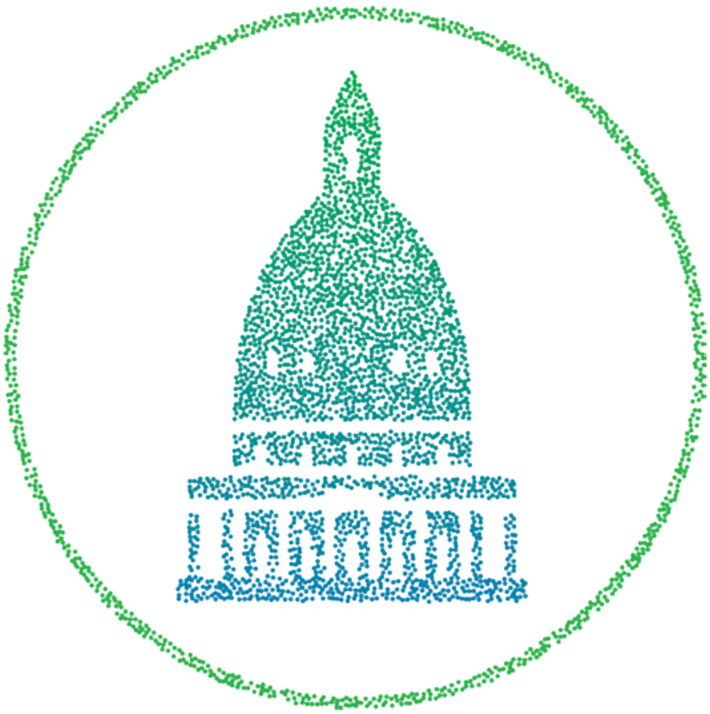
Tax-exempt bonds

The Act repeals tax credit bonds and advance refunding bonds, but it does not include provisions in the House bill that would have repealed private activity bonds and tax-exempt treatment of interest on professional sports stadium bonds.

Provisions not included

The Act does not include proposals from the House-approved bill that would have:

- Limited the exclusion of research income from unrelated business taxable income for certain tax-exempt organizations to income from publicly available research;
- Excluded certain entities from the definition of a "business enterprise" for purposes of the private foundation excess business holdings tax;
- Clarified that organizations (such as state pension funds) that are tax exempt or whose income is excluded from tax under a section other than section 501 (such as organizations that perform an essential governmental function that exclude income under section 115) and who have also obtained tax exemption under section 501(a) (so-called dual status organizations) are subject to the unrelated business income tax (UBIT) rules under section 511;
- Restructured the excise tax on private foundation investment income;
- Added new Form 990 reporting requirements for sponsors of donor advised funds;
- Provided that art museums will not qualify for private operating foundation status unless the museum is open to the public during normal business hours for at least 1,000 hours a year; and
- Temporarily allowed section 501(c)(3) organizations to make statements relating to a political campaign in ordinary course of their tax-exempt activities as long as they do not incur more than incidental incremental expenses.



Compensation and benefits provisions

The Act includes a number of provisions in the area of compensation and benefits that could have a significant impact on businesses as well as their employees.

Limitation on excessive employee remuneration

Before the new law was enacted, an employer generally could deduct reasonable compensation for personal services as an ordinary and necessary business expense. An explicit exception under section 162(m) limited the deductibility of compensation expenses by applicable employers whose securities are publicly traded in the United States. The otherwise allowable deduction for compensation with respect to a "covered employee" of a publicly held corporation was limited to no more than $1 million per year unless specific exceptions apply. Covered employees included the principal executive officer and next three highest paid employees as of the last day of the employer's taxable year. The principal financial officer (i.e., chief financial officer) was excluded from the definition of a covered employee.

The Act modifies those rules to:

- Repeal the performance-based compensation and commission exceptions to the section 162(m) $1 million deduction limitation.
- Expand the definition of applicable employer to entities that are either: (1) an issuer of securities that are subject to the registration requirements of section 12 of the Securities and Exchange Act of 1934 (the "1934 Act"), or (2) an issuer that is required to file reports under section 15(d) of the 1934 Act.
- Revise the definition of a covered employee to include both the principal executive officer and the principal financial officer. An individual is a covered employee if the individual holds one of these positions at any time during the taxable year. Further, the provision defines as a covered employee the three 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 for the taxable year, as well as officers of a corporation that are not required to file a proxy statement but which are otherwise included within the revised definition of an applicable employer. The provision includes officers of an applicable employer who would have been subject to proxy filing requirements but for special circumstances arising during the year that impacted the filing requirement.
- Provide that status as a covered employee continues after separation from service, including years after the death of the individual.

The provision applies to taxable years beginning after December 31, 2017. 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. 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. A contract that provides for use of discretion would likely not qualify for the transition rule. Any contract that is entered into on or before November 2, 2017, and that is renewed after that date will be treated as a new contract. Additionally, a contract that is terminable or cancellable without condition or consent by either or both parties will be treated as a new contract entered into on the date of any such termination or cancellation, if made, would be effective. A contract is not considered to be terminable or cancellable if terminated or cancelled only by terminating the employment relationship with a covered employee.

A provision in the Act that adds an excise tax on certain types of compensation paid by tax-exempt organizations is discussed in the tax-exempt organizations section of this publication.

Limitation on deduction by employers for fringe benefit expenses

The Act 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 (such as an airplane) used in connection with any of the above items. Thus, it repeals the prior-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, as well as the related rule applying a 50 percent limit to such deductions.

While the Act retains the 50 percent deduction for food and beverage expenses associated with the operation of a taxpayer's trade or business (e.g., meals consumed by employees on work travel), it expands the exception to the 50 percent limitation to employer expenses associated with providing food and beverages to employees through an eating facility that meets the requirements to be considered a de minimis fringe benefit under pre-enactment law.

The Act also disallows the deduction for expenses associated with providing any qualified transportation fringe to employees. In addition, the deduction for expenses incurred for providing transportation (or any payment or reimbursement) related to commuting between the employee's residence and place of employment, other than as necessary for ensuring the safety of an employee, is disallowed under the Act.

The Act 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.

A provision that subjects certain fringe benefits provided by tax-exempt organizations to Unrelated Business Income Tax (UBIT) is discussed in the tax-exempt organizations section of this publication.

Qualified equity grants

Under existing tax rules, nonstatutory stock options (i.e., options that are not incentive stock options or options granted under an employee stock purchase plan) granted at fair market value are generally not taxable until the exercise of the option if the service recipient receives fully vested stock. Additionally, restricted stock units (RSUs) that are exempt from, or comply with, the nonqualified deferred compensation rules under section 409A are generally not taxable until delivery of fully vested stock.

Under the Act, and in addition to the existing tax rules described in the preceding paragraph, a "qualified employee" may elect to defer the income attributable to a stock option or RSU received in connection with the performance of services for up to five years if the corporation's stock is an "eligible corporation." Instead of including income at exercise of a stock option (assuming fully vested stock is received) or at delivery of fully vested stock as required under current law, if the qualified employee makes a timely "inclusion deferral election," then the employee will be subject to income tax at the earlier of the following dates:

- The date the qualified stock is transferrable;
- The date the employee becomes an "excluded employee";
- The date on which any stock of the employer becomes publicly traded;
- Five years after the employee's right to the stock is substantially vested; or
- The date the employee revokes the election.

A qualified employee is generally an individual who is not an excluded employee and who agrees, in the inclusion deferral election, to meet the requirements necessary to ensure the income tax withholding requirements with respect to the qualified stock are met. An excluded employee includes the following:

- An individual who becomes a 1 percent owner during the taxable year;
- A 1 percent owner of the corporation at any time during the 10 preceding calendar years;
- The current or former chief executive officer or chief financial officer of the corporation (or an individual acting in either capacity);
- A family member of an individual described above;
- One of the four highest-compensated officers of the corporation during the taxable year; or
- The four highest-compensated officers of the corporation for any of the 10 preceding taxable years.

A corporation is an eligible corporation with respect to a calendar year if no stock of the employer corporation (or any predecessor) is readily tradable on an established securities market during any preceding calendar year. Additionally, the corporation must have 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 US possession) are granted stock options or RSUs with the same rights and privileges to receive qualified stock (the "80 percent requirement"). This test must be met with respect to options only or RSUs only, not a combination of the two. Note, the amount granted to each employee need not be identical under the plan.

Under the Act, corporations that are members of the same controlled group are treated as one corporation.

An inclusion deferral election must be made no later than 30 days after the first date the employee's right to the stock is substantially vested or is transferable, whichever is earlier. An election is generally made in the same manner as a section 83(b) election. An inclusion deferral election may be made on a statutory stock option (i.e., incentive stock options or options granted under an employee stock purchase plan). If an election is made with respect to a statutory stock option, then the option is not subject to the statutory stock option rules.

With respect to the employer's deduction, if an employee makes an inclusion deferral election, the employer's deduction is also deferred until the employer's taxable year in which or with which ends the taxable year of the employee for which the amount is included in the employee's income. Also, the inclusion deferral election affects only the deferral of income tax and does not affect the timing of FICA and FUTA.

The Act includes certain employee notice requirements. Specifically, a corporation that transfers qualified stock to a qualified employee must provide notice to the employee at, or a reasonable period of time prior to, the point qualified stock becomes substantially vested certifying that the stock is qualified stock. Additionally, the employee must be notified:

- That the employee may (if eligible) elect to defer income inclusion with respect to the stock;
- If the employee makes an inclusion deferral election, the income inclusion amount 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); and
- That the amount of income to be included at the end of the deferral period will be subject to withholding.

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.

The provision is generally applicable to options exercised, or restricted stock units granted, in 2018 and later taxable years.

The Act includes a transition rule providing that until regulations or other guidance implementing the 80 percent and employer notice requirements are issued, a corporation will be treated as complying with those requirements if it complies with a reasonable good-faith interpretation of the requirements.

Additionally, the provisions related to coordination with sections 83 and 409A are intended to be limited to the specific issues raised by coordination with section 83(i).

Retirement accounts

The Act includes provisions related to the recharacterization of IRA contributions and rollovers of retirement plan loan offsets.

- **Recharacterization of IRA contributions:** The bill includes a provision that restricts individuals from recharacterizing certain IRA contributions. Under current law, an individual who makes a contribution to one type of IRA (either traditional or Roth) is permitted to recharacterize that contribution and thereby have it treated as if made to the other type of IRA. An individual who chooses to recharacterize a contribution must do so no later than the extended due date of the tax return for the year the contribution is made. Before the new law was enacted, individuals were permitted to recharacterize either an annual IRA contribution or a traditional-to-Roth IRA conversion. The Act eliminates the ability to recharacterize traditional-to-Roth IRA conversions. As a result, once an individual has converted an amount in a traditional IRA to a Roth IRA, that conversion is irrevocable. Regular, annual IRA contributions, to either type of IRA, can still be recharacterized.
- **Rollovers of plan loan offsets:** The Act extends the rollover period for certain plan loan offsets. Normally, if a participant receives a distribution from a retirement plan, the distribution must be rolled over within 60 days of receipt, if not transferred directly to the other retirement plan. If an individual has an outstanding loan at the time of termination of employment, plans will often cancel the loan. This is referred to as a "plan loan offset" and is considered a distribution from the plan, which can be rolled over, but subject to the 60-day requirement applicable to all rollovers. Under the Act, if the individual has an outstanding loan when he or she terminates employment, the participant will now have until the extended due tax of his or her tax return for the year in which the offset occurs in order to roll over an amount equal to the outstanding loan balance. No change is made to any other rules applicable to rollovers.

Employer-provided reimbursements and awards

The Act modifies several deductions and exclusions related to various reimbursements and awards provided by employers to their employees.

- **Qualified bicycle commuting reimbursement:** The Act repeals the income and employment tax exclusion for qualified bicycle commuting reimbursements provided by an employer as payment for reasonable expenses such as bicycle purchase, repair, and storage. The provision is effective for taxable years beginning with taxable years on or after January 1, 2018, through December 31, 2025.
- **Qualified moving expense reimbursement:** The exclusion for qualified moving expense reimbursements provided by an employer to an employee is repealed under the enacted legislation except for members of the Armed Forces moving on military orders. The repeal applies for both income and employment tax purposes. The provision is effective for taxable years beginning on or after January 1, 2018, and sunsets on December 31, 2025.
- **Deduction for moving expenses:** The Act repeals the deduction for moving expenses. However, the deduction for expenses for in-kind moving and storage expenses provided to the Armed Forces (as well as their spouses and dependents) is retained. The provision is effective for taxable years beginning on or after January 1, 2018, and sunsets on December 31, 2025.
- **Employee achievement awards:** The Act defines "tangible personal property" that may be considered a deductible employee achievement award to exclude the following items: cash, cash equivalents, gift cards, gift coupons or gift certificates (other than arrangements conferring only the right to select and receive tangible personal property from a limited array of such items pre-selected or pre-approved by the employer), or vacations, meals, lodging, tickets to theater or sporting events, stocks, bonds, other securities, and other similar items. The provision is effective for taxable years beginning after December 31, 2017.
- **Length of service awards for bona fide public safety volunteers:** The Act increases the aggregate amount of length of service awards that may accrue for a bona fide volunteer with respect to any year of service to $6,000 and adjusts that amount in $500 increments to reflect changes in cost-of-living for years after the first year the Act is effective. If the plan is a defined benefit plan, the limit applies to the actuarial present value of the aggregate amount of length of service awards accruing with respect to any year of service. Actuarial present value is calculated using reasonable actuarial assumptions and methods, assuming payment will be made under the most valuable form of payment under the plan with payment commencing at the later of the earliest age at which unreduced benefits are payable under the plan or the participant's age at the time of the calculation. The provision is effective for taxable years beginning after December 31, 2017.

Tax compliance and procedural provisions

The Act modifies several provisions related to tax preparer due diligence requirements, return filing requirements, and IRS levies.

Tax return preparer due diligence for filing status and certain credits

The Act amends section 6695(g) to apply a due diligence requirement to tax return preparers when determining the eligibility of a taxpayer to file as head of household, as well as eligibility for or amount of the child tax credit, Hope and lifetime learning credits, and the earned income credit. Failure to meet the due diligence requirements, which are to be set forth in regulations, results in a penalty of $500 per violation. The provision applies to tax years beginning after December 31, 2017.

Wage, salary, or other income exemption from IRS levy

The Act modifies the exempt amount of wages, salary, or other income ("wage exemption") for IRS levies under section 6334(d) for tax years in which the personal exemption is suspended. During this period, the wage exemption is $4,150 multiplied by number of dependents plus the standard deduction, divided by 52, subject to inflation adjustments.

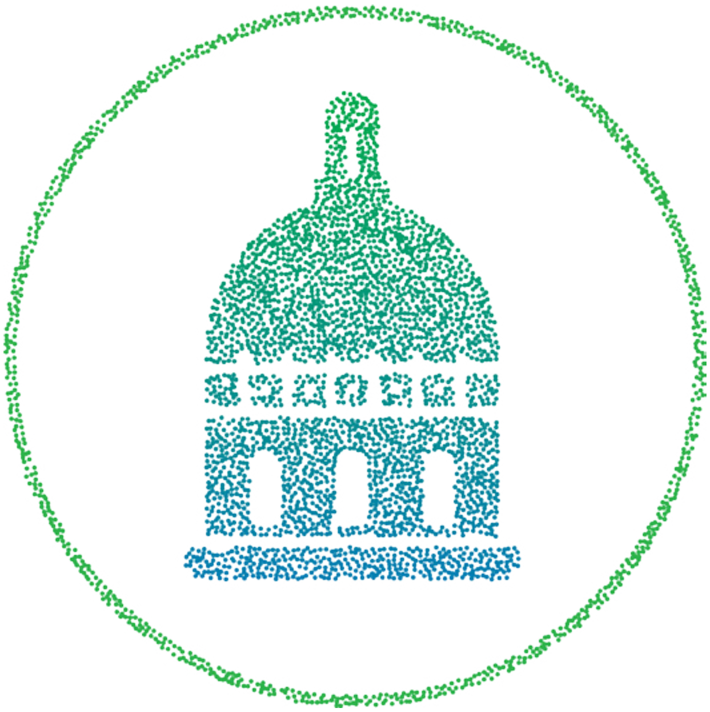
Individual income tax filing requirements

The Act modifies section 6012 for tax years beginning after December 31, 2017, and before January 1, 2026. Under section 6012 every individual who has gross income for the taxable year is required to file an income tax return unless gross income is below certain specified dollar thresholds. An individual who is not married is not required to file a return unless the individual's gross income for the year exceeds the standard deduction. Married individuals filing jointly are not required to file a return if their combined gross income is less than the standard deduction applicable to a joint return, provided that: (1) at close of the taxable year they had the same household; (2) neither spouse makes a separate return; and (3) neither is a dependent of another taxpayer who has income (other than earned income) in excess of $500 (indexed for inflation).

Extension of time limit for contesting IRS levies

Section 6343 currently provides that if the IRS determines that property has been wrongfully levied upon, then the IRS can return to the taxpayer: (1) the specific property levied upon; (2) an amount of money equal to the amount of money levied upon; or (3) an amount of money equal to the amount of money received by the United States from a sale of such property. The specific property may be returned to the taxpayer at any time. If the property has been sold, then there is a nine-month period from the date of the levy to return to the taxpayer an amount equal to the amount of money levied upon or received from such sale. The Act extends the nine-month period to two years. This provision applies to levies after the enactment date of the bill and levies made within nine months prior to enactment.

In addition, the Act extends the time periods in section 6532 to two years for filing a suit related to a levy. This provision applies to levies after the enactment date of the Act and levies made within nine months prior to enactment.



Financial reporting implications

President Trump signed the Act into law on December 22, 2017, and that action constitutes enactment of the law as contemplated by ASC 740. Accordingly, entities will need to account for the effects of the change in tax law effective in the quarter that includes December 22, 2017.

The US Securities and Exchange Commission, however, has also provided regulatory guidance (Staff Accounting Bulletin No. 118, "SAB 118") regarding the accounting impacts of the new law. The guidance contained within SAB 118 follows an implementation approach whereby entities would follow something similar to the measurement period in a business combination. More specifically, an entity would recognize those matters for which the accounting can be completed, as might be the case for the effect of rate changes on deferred tax assets and deferred tax liabilities. For those matters that have not been completed, the entity would recognize provisional amounts and then adjust them over time as more information becomes available, along with robust disclosures.

Tax law changes with significant financial statement impact

The Act includes significant changes to US tax law and will have a significant impact on companies' financial statements. We expect the more significant impacts to include the following:

- Deferred tax assets and liabilities (DTAs and DTLs), including those related to items initially recorded through other comprehensive income and shareholders' equity, will need to be remeasured for the impact of the corporate rate reduction, and any adjustments are included in income from continuing operations for the period that includes the enactment date.
- For a fiscal-year-end entity, pursuant to IRC section 15, a blended tax rate will apply to the taxable year that includes the enactment date. Accordingly, deferred taxes as of the enactment date for a fiscal-year-end entity that are expected to reverse in the current fiscal year should be measured at the blended tax rate and those expected to reverse in future years should be measured at the new 21 percent statutory rate. The effect of this remeasurement is recorded discretely in the period of enactment. The effect of the tax rate change on taxes currently payable or refundable is reflected after the effective dates prescribed in the statutes in the computation of the annual effective tax rate beginning no earlier than the first interim period that includes the enactment date of the new legislation. Because the tax rate reduction is administratively applied to an entity with a fiscal year-end by applying the blended tax rate to the taxable income for the full fiscal year, the change in tax rate is effective at the beginning of the fiscal year.
- An entity that historically asserted that it is indefinitely reinvested in the outside basis difference in a foreign subsidiary or foreign corporate joint venture that is essentially permanent in duration will likely be required to recognize a liability on account of the provision mandating a deemed repatriation of foreign earnings and profits. Entities that had not previously determined that they were indefinitely reinvested in the outside basis difference in a foreign investment will likely need to remeasure existing deferred tax liabilities recognized for the foreign investment because the tax due as a result of this provision will likely be different than the tax liability that would have been due if the outside basis difference reversed under prior law. If the entity elects to pay the related tax liability over an eight-year period, a portion of the liability may be classified as noncurrent.
- A US entity may experience an increase in US taxable income under anti-base erosion provisions. Additionally, certain global intangible low-taxed income will be currently taxable and payments to related foreign parties will not be deductible under the Base Erosion and Anti-Abuse Tax. These provisions could impact an entity's prospective effective tax rate. The entity will need to consider whether and how US deferred taxes should be recorded if it expects to have a taxable income inclusion under the GILTI provision or have income subject to the new BEAT provisions.
- Several provisions in the new law either eliminate or limit deductions and tax credits (e.g., interest expense limitations, modifications to net operating losses, loss of business deductions and credits) that could unfavorably affect an entity's effective tax rate and negatively impact earnings. These provisions, as well as those discussed above, could also affect valuation allowance analyses and related disclosures.

To the extent potential income tax reform could materially affect the company or its business, SEC registrants should also consider possible disclosure requirements under Risk Factors and Management's discussion and analysis of financial condition and results of operations.

Frequently asked questions

A financial reporting alert dated January 3, 2018, and prepared by the ASC 740 group at Deloitte Tax addresses a number of frequently asked questions related to the accounting implications of the Act.

State business tax issues raised by federal tax reform

The enactment of tax reform legislation and its sweeping revisions to the federal income tax system also will have major impacts on state governments across the country. For example, the reduction in the corporate tax rate from 35 percent to 21 percent may encourage companies to make federal elections between now and the end of their tax year, for which the state tax consequences should be considered. Other changes can be expected to affect the calculation of federal taxable income, which is used by a number of states as the starting point for calculating state taxable income. Finally, several of the provisions contained in the Act are designed to stimulate investment in the US economy, which may also have a significant impact on the states.

The focus here is on those provisions in the Act that are likely to generate the most immediate interest from a state and local tax perspective for businesses. From a state budgetary perspective, it is anticipated that states' requirements to run balanced budgets may result in disparate levels of legislative conformity among them. It is conceivable that some states may even choose to lag in conformity, possibly necessitating a federal pro forma starting point consistent with prior federal law. As a result, more diligence than ever may be required to effectuate compliance with the varied permutations of state tax conformity.

However, it should not be presumed that state legislative action necessarily precedes any state consequences resulting from these federal changes. Certain states automatically conform to federal changes and absent proactive legislative decoupling, companies can expect certain state consequences to result at the same time as the federal consequences on the day of enactment (Day One). Accordingly, on Day One, companies will need to analyze and assess the financial implications of state conformity to these changes, based on each company's distinct state tax filing footprint.

Reduction in federal corporate rates

The Act reduces the corporate income tax rate from 35 percent to 21 percent for tax years beginning after December 31, 2017. Based on this tax rate decrease, it is reasonable to expect certain companies to seek to accelerate deductions and defer income in order to capitalize on the tax rate reduction. For state income tax purposes, companies should evaluate how any such expense acceleration or deferral of income would impact any deferred state tax assets and liabilities (and any related valuation allowances) they may have and continue to monitor for additional considerations.

New deduction for pass-throughs

The Act also provides for a new deduction for pass-through businesses equal to 20 percent of the pass-through entity's "qualified business income," which is embodied in new section 199A. (See the pass-throughs chapter in this publication for additional discussion.) The states will need to evaluate whether they wish to conform to this new deduction. Budgetary pressures may lead various states to decide that conformity to the new deduction may be too expensive.

Limitation on interest expense deduction

The Act provides that companies (regardless of their legal entity form) will not be able to deduct their net interest expense to the extent it exceeds 30 percent of the taxpayer's adjusted taxable income. Various exceptions and modifications apply (e.g., small taxpayers with average annual gross receipts of $25 million or less for a specified three-year time period).

States with rolling conformity will conform to this new limitation on the interest expense deduction on Day One; others, if they update their conformity provisions. Furthermore, states with differing filing groups (e.g., separate returns) arguably may need to apply this new limitation on a separate company rather than on an affiliated group/consolidated return basis. In any event, we would generally expect states' scrutiny of interest expense deductions to continue.

Immediate expensing

As noted in the chapter on business tax issues, the Act increases the bonus depreciation amount provided by section 168(k)(1)(A) to 100 percent (from 50 percent under prior law) for property placed in service after September 27, 2017, and before January 1, 2023. The percentage subsequently declines by 20 percentage points each year until it reaches 20 percent for property placed in service after December 31, 2025, and before January 1, 2027. The state tax issues presented by these proposals include:

- **State conformity:** A majority of the states decouple from federal bonus depreciation, though "rolling conformity" states that currently conform to section 168(k) will automatically conform to this amendment absent the state adopting specific legislation disconnecting from the federal provision. Decoupling could span a range of options at the state level, including a complete decoupling, retaining the prior-law 50 percent limitation, or other state-specific modifications. Companies should evaluate state consequences as of Day One and then continue to monitor additional consequences as additional states decide whether to conform to or decouple from immediate expensing.
- **State credit and incentive opportunities:** The full expensing provisions may encourage investment in capital assets across the United States. Many states offer statutory credits as well as discretionary incentives for this type of investment. Companies who may plan on making an investment to capitalize on the federal benefit from immediate expensing should consider whether any state and/or local incentives may be available prior to deciding where to make this investment. These incentives are not limited to income/franchise taxes, but may include (1) sales and use taxes, (2) property taxes, (3) employment/payroll taxes, and (4) nontax incentives such as zoning and permitting assistance. However, to the extent a state incentive incorporates federal adjusted basis in its asset qualification rules, eligibility may need to be reconsidered.

Modification of net operating losses

The Act provides for the general elimination of most net operating loss carrybacks and limiting the NOL deduction prospectively to 80 percent of the taxpayer's pre-NOL taxable income. Most states already impose their own specific NOL deduction rules and we would expect that practice to continue. Certain states (e.g., Delaware, Louisiana, Maine, Maryland, and Virginia) do conform in various respects to the federal NOL deduction currently. Any rolling conformity states in this group would automatically conform and would need to enact legislation to decouple.

Various other base-broadening provisions

Other provisions of the Act contain base-broadening provisions that are beyond the scope of this discussion. Companies will need to evaluate the state consequences of these provisions on Day One as well. These include but are not limited to:

- Limitation on like-kind exchanges under section 1031;
- Repeal of the deduction for domestic production activities under section 199(a);
- Limitation on entertainment and similar expenses; and
- Reform of various federal business and energy credits, bond provisions, etc.

Taxation of foreign operations

Some of the most far-reaching provisions in the Act pertain to the US taxation of foreign operations. These changes, which are discussed in greater detail in the chapter on international tax provisions, include, but are not limited to:

Participation exemption for foreign dividends: Unlike prior law, which generally provided for deferral except for under certain circumstances, the Act exempts 100 percent of the foreign-sourced portion of dividends paid by a foreign corporation to a US corporate shareholder that owns 10 percent or more of the foreign corporation. Most states that include foreign dividends in the tax base extend their own dividends received deduction, though the deduction modification offered by specific states may not be as generous as the new participation exemption. In addition, some states only grant a DRD for dividends paid by more than a fixed percentage (e.g., more than 50 percent-owned) subsidiaries and thus may offer no deduction. Depending on whether a state starts with federal taxable income before or after certain deductions, such as DRDs, and which DRDs are picked up, automatic conformity states may or may not pick up the 100 percent exclusion. This may be an area to monitor for potential future state legislation.

Transition tax/deemed repatriation: The Act requires a US shareholder owning at least 10 percent of the vote of a foreign subsidiary (where there is at least one US corporation that is a 10 percent voting shareholder) to add to its subpart F income the shareholder's pro rata share of the foreign subsidiary's net post-1986 historical E&P, as determined as of November 2, 2017, or December 31, 2017, whichever is higher. This income is to be reported as of the foreign subsidiary's last tax year beginning before 2018, and is taxed at one of two rates: (1) 15.5 percent for E&P held as cash or cash equivalents; and (2) 8 percent for all other E&P.

These rates were increased from the proposals made in both the original House and Senate tax reform bills. The increase in these rates will not have a direct impact on the states as the states will impose their own rates on this income to the extent the income is taxable by the states. The Act also provides that the taxpayer may elect to pay this liability in installments; such provisions would not seem to carry over at the state level absent legislative action.

This deemed repatriation is subject to several complex adjustments (e.g., netting E&P surpluses and deficits). However, the deemed repatriation raises a number of significant state issues, including whether and how the respective states tax subpart F income. The concept behind the deemed repatriation is that once the federal tax is paid on the deemed repatriation, the actual repatriation of these amounts will be tax-free at the federal level. One key issue for companies to consider is, to the extent a particular state does not tax the deemed repatriation, whether such a state will attempt to tax the funds upon their actual repatriation. Another issue for companies to consider is whether the company has already paid state income tax on any of this E&P (e.g., by filing a worldwide state income tax return) and, if so, whether this presents a basis to exclude the deemed repatriated dividends from income.

It is also anticipated by the proponents of the Act that a substantial portion of the E&P subject to the deemed repatriation will be repatriated to and reinvested in the US economy. This proposal works in conjunction with the immediate expensing of capital expenditures for five years provision discussed above. Accordingly, companies who anticipate repatriating and reinvesting a substantial amount of E&P following the deemed repatriation should consider state and local credits and incentives opportunities for such reinvestment, which often take time to secure.

The potential state tax treatment of this deemed repatriation varies. Some states have a fairly straightforward approach for taxing or exempting the addition to subpart F income. For example, a rolling conformity state such as Oregon may conform to the amended section 965 immediately upon enactment. Oregon also provides a fairly broad provision that would appear to grant an 80 percent DRD on this addition to income. Other states, such as California, which employs a selective incorporation approach to IRC conformity, may not explicitly conform to section 965, leaving out the addition, or at least leaving it in question. The potential for inconsistent treatment from one state to the next must be carefully evaluated.

Current taxation of global intangible low-taxed income: The Act includes in gross income of a US shareholder of a CFC its global intangible low-taxed income. Such GILTI, subject to complex calculations and deductions (e.g., a deduction is provided equal to 50 percent of the taxpayer's GILTI) for corporate shareholders is subject to an effective tax rate of 10.5 percent. These provisions are intended to prevent against erosion of the US tax base. The states, particularly those that currently use a water's edge filing group, may need to determine the appropriateness of conforming to such changes. This gross income inclusion seems on its face to be likely to be included in state taxable income, but the deductions need to be carefully evaluated for state purposes in areas of inapplicability (e.g., offset for foreign tax credits).

Base Erosion and Anti-Abuse Tax: The Act imposes a new excise tax on a taxpayer's "base erosion minimum tax amount," for each taxable year. The provision attempts to prevent deductions for "base erosion payments" made by domestic companies to foreign affiliates. Unlike the new provision for the current taxation of GILTI, we would anticipate the BEAT will have less applicability to the states since it does not directly affect the calculation of federal taxable income (i.e., the starting point for calculating state taxable income in most states).

Considering the state implications of federal reform provisions

Companies evaluating the state tax consequences of these changes may want to consider the following:

ASC 740 considerations: A threshold issue for most state tax issues presented by federal tax reform is assessing state conformity to the Internal Revenue Code and the attendant ASC 740 implications this may trigger. (See the chapter on business tax issues for a discussion of ASC 740 issues generally.)

Taxpayers should review when and how the state conforms to changes in the Internal Revenue Code and evaluate whether and how the state-specific conformity provisions impact the company's state current and deferred taxes. For example, companies may need to review their state tax attribute carryforward schedules (e.g., state credits, net operating losses, etc.) and consider how these attributes will be affected by potential base broadening in conformity states and any federal income tax planning they may be considering for purposes of the valuation allowance analysis.

The federal tax effect of state uncertain tax positions may also need to be revalued if the new lower federal tax rate will be applicable in the period the state taxes are deductible.

Choice of entity: Given the reduction in federal corporate income tax rates, the modification or elimination of many federal incentives and the new deduction for pass-through businesses, some companies may consider structuring and choice-of-entity options. Any such decisions should be made only after careful consideration of the state income tax issues presented, including whether the states at issue impose entity-level taxes on pass-through businesses.

State considerations of new categories of subpart F income: The Act includes both an amended section 965 and a new section 951A. Certain states may not conform to these new/amended Internal Revenue Code sections without first adopting updated conformity legislation. In addition, certain states (e.g., Florida and New York) may have seemingly adopted only portions of the subpart F provisions leaving incomplete guidance and issues to work out. Distinctions between the states may seem subtle but could in fact result in disparate state income tax consequences.

State ability to tax additions to income under section 965: As a matter of tax policy, there is a question of whether states should be able to tax the deemed addition to federal taxable income resulting from the new section 965. Generally speaking, many states do not tax deemed distributions of domestic earnings and profits—it may be questionable whether states may do so for foreign E&P. And whether companies will make actual distributions of the foreign E&P that will comprise the measure of the addition to subpart F income remains a company by company determination. Accordingly, the ability of states to tax this income remains an open question, even if the states are merely attempting to conform to the amendments to the Internal Revenue Code.

Apportionment considerations: States may treat the addition to subpart F income under either the addition under section 965 or the GILTI provisions as outside the definition of apportionable sales. For example, to the extent the addition to subpart F income is treated as a dividend, some states may exclude dividends from the sales factor while other states may include only a portion. Furthermore, states may have provisions denying factor representation for licensing of intangibles where the activity at issue generates GILTI (i.e., the market for the licensing may not be readily determinable). Such provisions would need to be closely analyzed.

Inconsistency between federal and state ownership thresholds for deemed dividend: In the amended federal income tax provisions affecting the deemed repatriation of foreign E&P and the new participation exemption that will apply prospectively, the federal provisions often turn on an ownership threshold of 10 percent. This threshold is far lower than the ownership thresholds that states often require for determination of unitary/combined groups (e.g., 50 percent or 80 percent, depending on the state).

Evaluating Day One impact

While this discussion is not an exhaustive list of all state tax issues raised by each provision in the Act, it is intended to provide an overview of the range of state and local tax issues that are presented by the change in federal tax law. A company will need to consider some or all of these state and local tax issues when evaluating the Day One impact of the Act on current and prospective tax planning.

Looking ahead

Now that the tax reform legislation has been enacted into law, congressional leaders may have to spend a good part of the coming year(s) making modifications to ensure it works as intended.

Technical corrections

House Ways and Means Committee Chairman Kevin Brady, R-Texas, has already acknowledged that what is known as "technical corrections" legislation likely will be required in 2018—a not-surprising outcome given the Act's size and complexity, as well as the speed with which it was enacted.

Historically, technical corrections bills have been relatively noncontroversial, seeking to fix typographical errors in the legislative language, clarify legislative intent with respect to particular provisions, or make conforming changes to related sections that may have been left out of the original bill. As a general matter, because technical corrections do not reflect changes in legislative intent, the Joint Committee on Taxation does not assign a revenue impact to such provisions—though it should be said there is no requirement that all provisions moved in a technical corrections package be entirely nonsubstantive. (It is, after all, a regular piece of legislation at its core.)

Moreover, technical corrections bills generally have been advanced with the blessing of both the chairman and ranking member of the two congressional taxwriting committees—giving them an aura of bipartisanship that has often helped to shuttle them through Congress without much controversy.

Will there be bipartisan cooperation?

But some Democrats already are signaling they may not be inclined to lend their support to any future efforts to patch up the GOP tax reform bill. Others see an opportunity for political payback, noting Republicans' lack of cooperation in fixing elements of the Patient Protection and Affordable Care Act, which moved through Congress in 2010 with only Democratic support.

It is also worth noting that, unlike the new tax reform law—which was moved under budget reconciliation and thus protected from a Senate Democratic filibuster—technical corrections legislation very likely cannot be moved under that process on account of the Senate's so-called Byrd Rule which, among other things, requires that provisions in a reconciliation bill have budgetary effect. This requirement can be waived with a three-fifths vote, but that outcome may not be likely given the highly partisan nature of the current tax debate.

Therefore, in practice, even if Republicans this year adopt a fiscal year 2019 budget resolution with reconciliation instructions allowing the movement of additional tax legislation on a filibuster-proof basis—a possibility Chairman Brady has alluded to—those instructions likely would have to be used only for substantive tax changes with nonincidental revenue implications. Moreover, the Senate's already narrow majority has now gotten even narrower: Alabama recently elected Democrat Doug Jones to fill the remainder of the unexpired term of now-Attorney General Jeff Sessions, and Jones was sworn in on January 3, 2018, replacing appointed Republican Sen. Luther Strange. That changes the Senate headcount to 51 Republicans and 49 Democrats, which means that passing a budget reconciliation bill with GOP votes alone may prove exceedingly difficult.

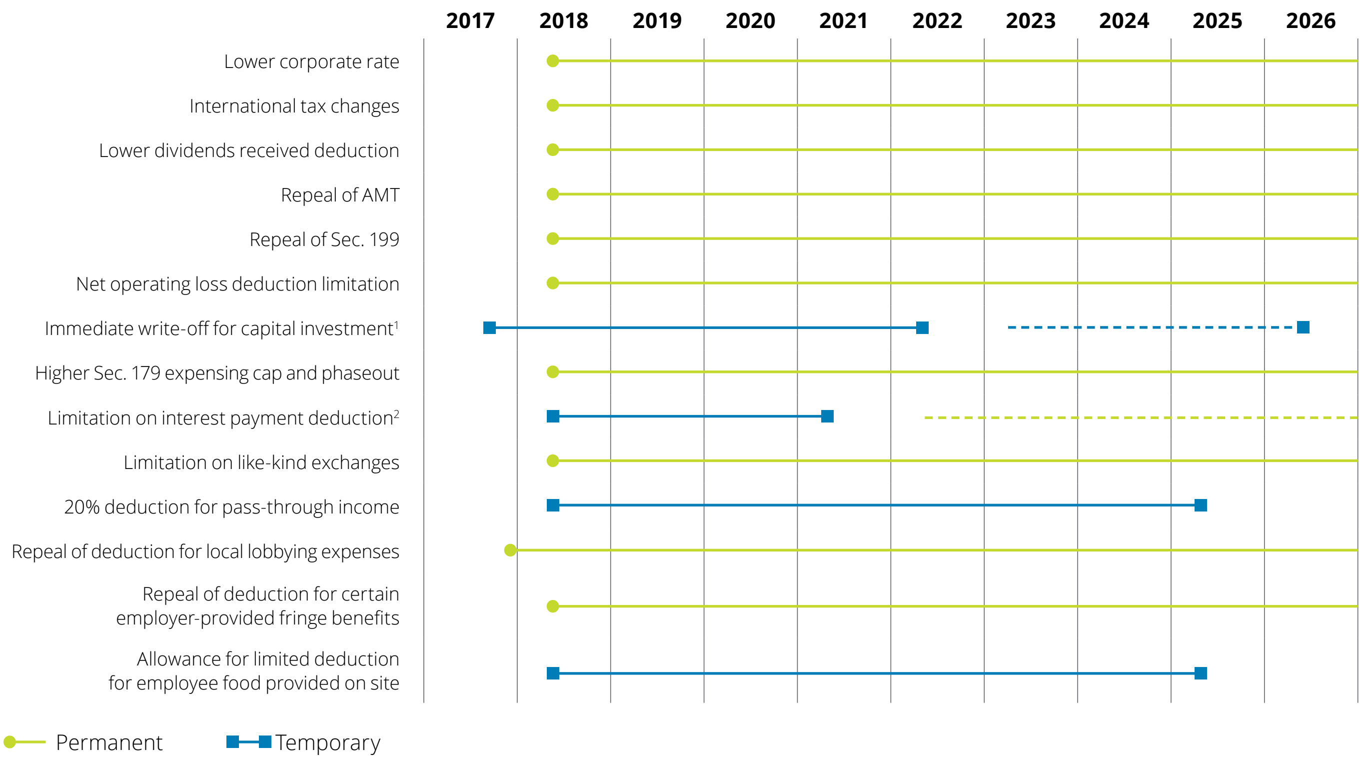
As a result of those challenges, we can expect a concerted effort by the administration, notably the Treasury Department, to issue regulations and guidance intended to ensure the smoothest possible implementation of the Act, as it was one of the president's signature achievements in his first year in office.

Appendices

2017 tax reconciliation bill: Effective dates

The charts that follow show the effective dates—and, in some cases, the scheduled expiration dates—of notable business and individual provisions in the new tax reform law.

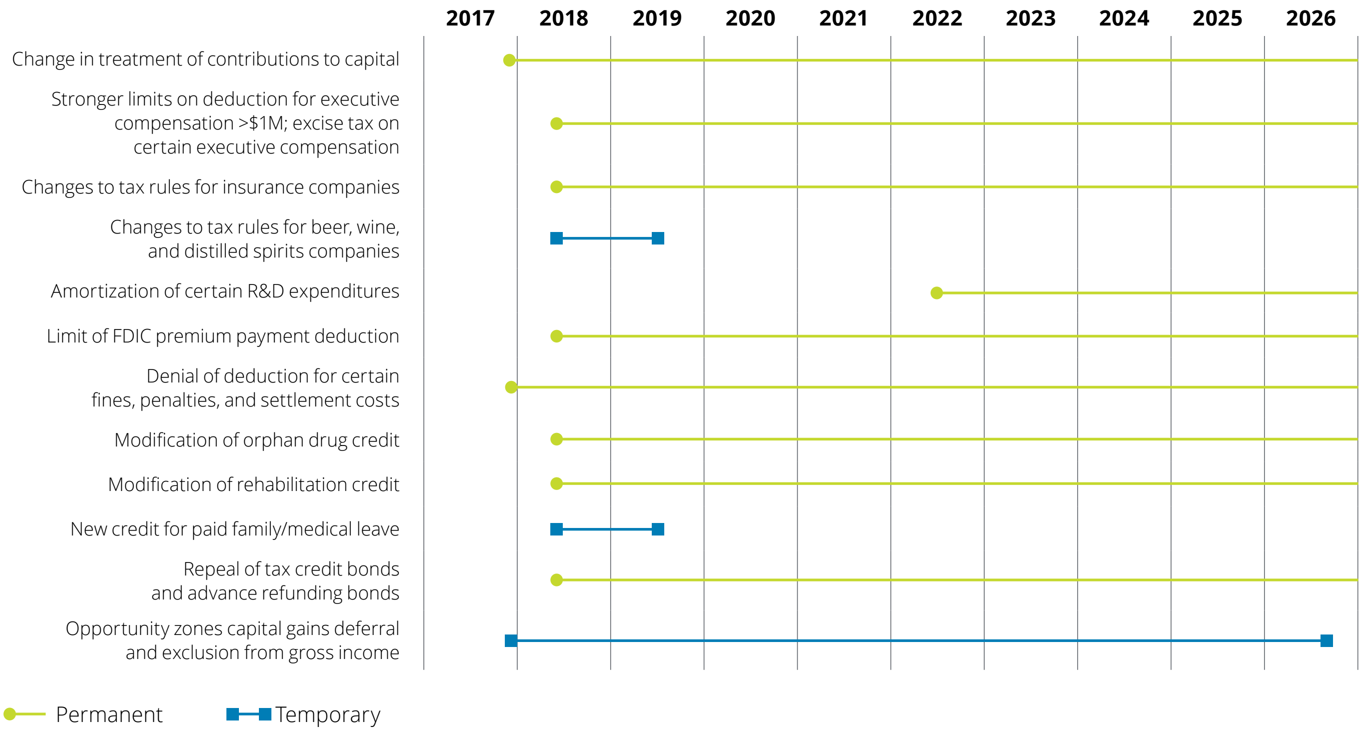
Business taxation



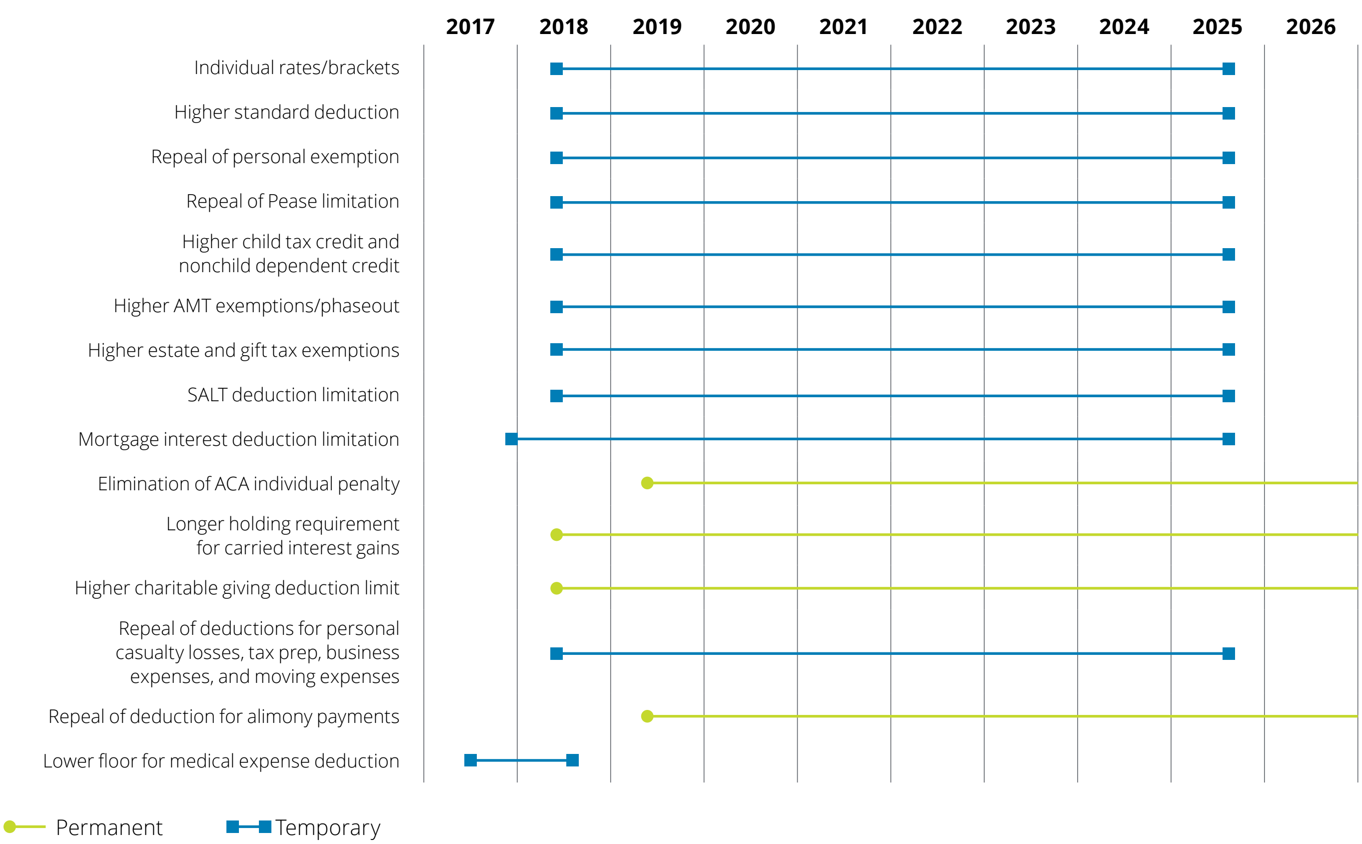
1. Permitted first-year write-off phases down 2023-2026

2. Stricter limitation after 2021

Business taxation



Individual taxation



How Congress got to 'yes': Tax reform provisions compared

The tables that follow compare the provisions in the tax reform law as enacted with those in the House version of the bill (approved on November 16, 2017), the Senate version (approved on December 2, 2017), and the Internal Revenue Code provisions in effect for 2017.

Business provisions in general

Business provisions in general				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
Corporate income	35% top rate; personal service corporations taxed at 35%	20% flat rate; 25% for personal services corporations; effective for tax years beginning after Dec. 31, 2017 Section 15 specifically applies to fiscal year-ends to obtain benefit of the reduced rate starting Jan. 1, 2018	20% flat rate; effective tax years beginning after Dec. 31, 2018 Section 15 not explicitly mentioned; appears to apply to corporate rate reduction No special rate for personal service corporations	• 21% flat rate; effective tax years beginning after Dec. 31, 2017 • Section 15 treatment appears same as Senate bill • No special rate for personal service corporations
Pass-through income	Taxed at owner's individual rate	25% rate on qualified business profits, generally consisting of 100% of any net business income derived from any passive business activity and a portion (based on a "capital percentage") of any net business income derived from any active business activity • Capital percentage generally equals 30%, but a taxpayer may elect to establish a higher percentage based on its facts and circumstances • 0% capital percentage assumed for specified service businesses • Activity-by-activity determination • REIT dividends eligible for 25% rate	23% deduction for domestic business profits, limited to 50% of W-2 wages after wage limitation phase-in • Specified service businesses generally not eligible, except for taxpayers with taxable income <$250K (single)/$500K (joint) (deduction phased out over the next $50K/$100K) • W-2 wage limitation phased in for taxpayers with taxable income >$250K/500K (over the next $50K/$100K) • Special rules apply to certain income from PTPs and dividends from REITs • Trusts and estates not eligible for the deduction • Sunsets Dec. 31, 2025	20% deduction for domestic business profits, limited to greater of (1) 50% of W-2 wages or (2) 25% of W-2 wages plus 2.5% of the unadjusted basis of qualified property after wage limitation phase-in • Specified service businesses generally not eligible, except for taxpayers with taxable income <$157.5K/$315K (deduction phased out over the next $50K/$100K) • W-2 wage limitation phased in for taxpayers with taxable income >$157.5K/315K (over the next $50K/$100K) • Special rules apply to certain income from PTPs and dividends from REITs • Trusts and estates are eligible for the deduction • Sunsets Dec. 31, 2025
Corporate dividends received deduction	70% deduction; 80% if received from a 20%-owned corporation	Reduced to 50% deduction and 65% deduction, effective for tax years beginning after Dec. 31, 2017	Reduced to 50% deduction and 65% deduction, effective for tax years beginning after Dec. 31, 2018	Reduced to 50% deduction and 65% deduction, effective for tax years beginning after Dec. 31, 2017
Corporate AMT	20% on alternative minimum taxable income	AMT repealed, effective taxable years beginning after Dec. 31, 2017 For tax years 2019 to 2021, AMT credit utilization limitation is increased by 50%, and AMT credit carryforward becomes a refundable credit For tax years beginning in 2022, AMT credit utilization limitation is increased to 100%	Retains current law	AMT repealed, effective tax years beginning after Dec. 31, 2017 For tax years beginning in 2018 to 2020, AMT credit utilization limitation is increased by 50%, and AMT credit carryforward becomes a refundable credit For tax years beginning in 2021, AMT credit utilization limitation is increased to 100%

Business provisions in general				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
Business interest payments	Generally deductible Section 163(j) limits the deduction for interest paid or accrued by certain corporations (where no US federal income tax is imposed on the interest income) whose debt-to-equity ratio exceeds 1.5 to 1.0, and where net interest expense exceeds 50% of its adjusted taxable income	Limited to business interest income + 30% of adjusted taxable income (ATI) ATI is computed without regard to any (1) item of income, gain, deduction, or loss, which is not allocable to the trade or business; (2) business interest income or expense; (3) net operating losses; and (4) depreciation, amortization, and depletion 5-year carryforward for disallowed amounts, treating business interest allowed as a deduction on a first-in, first-out basis Exemptions for real estate, farming businesses, and certain public utilities, retail floor planning indebtedness, small business, and for interest allocable to performing services as an employee Carryforward would be treated as a section 381(c) attribute and a pre-change loss for purposes of section 382(d)	Limited to business interest income + 30% of ATI ATI is computed similar to the House but takes into account depreciation, amortization, and depletion, and backs out any deductions taken under section 199 or 199A Indefinite carryforward for disallowed amounts Exemptions, at the taxpayer's election, for real estate and farming businesses and automatic exemptions for certain public utilities, retail floor planning indebtedness, small business, and for interest allocable to performing services as an employee Carryforward would be treated as a section 381(c) attribute and a pre-change loss for purposes of section 382(d)	Limited to business interest income + 30% of ATI ATI is similar to Senate but without regard to depreciation, amortization, or depletion only for taxable years beginning after Dec. 31, 2017 and before Jan. 1, 2022, and for tax years on or after Jan. 1, 2022, ATI is computed with depreciation, amortization, or depletion Indefinite carryforward for disallowed amounts Exemptions the same as the Senate bill, but with House definition of small businesses and a modified definition for floor plan financing Carryforward would be treated as a section 381(c) attribute and a pre-change loss for purposes of section 382(d)
Net operating loss deduction	2-year carryback and 20-year carryforward allowed to offset taxable income	NOL carryback period is eliminated and carryforward period is indefinite for NOLs arising in tax years beginning after Dec. 31, 2017 NOLs arising in tax years beginning after Dec. 31, 2017 receive annual escalator equal to 4% plus AFR NOL utilization is limited to 90% of taxable income for tax years beginning after Dec. 31, 2017 Transition Rule: For tax years which include Sep. 28, 2017 to Dec. 31, 2017, NOLs attributable to increased expensing as amended under section 168(k)(1)(A) are not eligible for carryback	NOL carryback period is eliminated and NOL carryforward period is indefinite for NOLs arising in tax years ending after Dec. 31, 2017 NOL utilization is limited to 90% of taxable income for NOLs arising in tax years beginning after Dec. 31, 2017 to Dec. 31, 2022 Limitation becomes 80% for NOLs arising in tax years beginning after Dec. 31, 2022	Same as Senate bill but with 80% utilization in place for losses arising in tax years beginning after Dec. 31, 2017
Capital contributions	Not included in gross income in transferee corporation	Gross income includes capital contributions, to the extent stock is not issued in exchange for contribution Similar rules applied to noncorporate entities Section 108(e)(6) also repealed Effective after the date of enactment	Not included	Preserves tax-free treatment for capital contributions but provides that such term does not include (1) contributions in aid of construction or any other contribution as a customer or potential customer, and (2) any nonshareholder contribution by any governmental entity or civic group Generally effective for 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

Business provisions in general				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
FIFO method for stock dispositions	Taxpayers may specifically identify shares of stock disposed of to determine cost basis (with FIFO method generally applicable)	No provision	Eliminates specific identification and generally adopts FIFO method to determine cost basis of specified securities on disposition Effective for dispositions after Jan. 1, 2018	No provision
Capital expensing	MACRS/ADS with bonus depreciation; or accelerated use of AMT credits; additional first-year depreciation deduction is allowed equal to 50% of the adjusted basis of qualified property acquired and placed in service before Jan. 1, 2020, with a phasedown for most property placed in service beginning after Dec. 31, 2017	100% immediate expensing for qualified property through 2022 Qualified property includes used property acquired by the taxpayer, provided property not used by taxpayer before it was acquired Qualified property excludes certain regulated utility property, property used in a real property trade or business, and property with floor plan financing indebtedness	100% immediate expensing for qualified property through 2022, then phased down annually through 2026 (80% in 2023, 60% in 2024, 40% in 2025, 20% in 2026); phaseout for property with longer production periods begins a year later Qualified production property excludes certain public utility property and certain property with floor plan indebtedness, but expanded to include qualified film, TV, and live theatrical productions	100% immediate expensing for qualified property placed in service from Sep. 27, 2017 through 2022, then phased down annually through 2026 (80% in 2023, 60% in 2024, 40% in 2025, 20% in 2026); phaseout for property with longer production periods begins instead in 2024 Qualified property includes used property acquired by the taxpayer, provided property not used by taxpayer before it was acquired
Manufacturing deduction (sec. 199)	Up to a 9% deduction on qualified production activity income; deduction to incentivize domestic production activities	Repealed for tax years after Dec. 31, 2017	Repealed for non-C corporation taxpayers for tax years after Dec. 31, 2017; C corporations repealed for tax years after Dec. 31, 2018	Repealed for tax years after Dec. 31, 2017
Like-kind exchanges	No gain or loss recognized for wide range of property held for productive use or investment Different classes of property include (1) depreciable tangible personal property; (2) intangible or nondepreciable personal property; and (3) real property	No gain or loss recognition allowed only for real property	No gain or loss recognition allowed only for real property not held primarily for sale	No gain or loss recognition allowed only for real property not held primarily for sale; transactions begun before Dec. 31, 2017 can be completed
Research and experimentation (R&E) expenditures	Section 174 provides an option to immediately deduct or amortize R&E related expenses over 5 years	Existing rules would continue to apply; however, section 174 expenditures paid or incurred in taxable years beginning after Dec. 31, 2022, are subject to capitalization and amortization over 5 years for research conducted within the US and 15 years for research conducted outside the US Modified cut-off 481(a) adjustment	Existing rules would continue to apply; same provisions as the House bill with regard to capitalization and 5-year or 15-year amortization of section 174 expenditures except applicable to amounts paid or incurred in taxable years beginning after Dec. 31, 2025	Existing rules would continue to apply; however, section 174 expenditures paid or incurred in taxable years beginning after Dec. 31, 2021, are subject to capitalization and amortization over 5 years for research conducted within the US and 15 years for research conducted outside the US Change applied on a cutoff basis
Small business election to expense depreciable business assets	Section 179 allows a current deduction for eligible property; $500K limit in a given year, phased out when the cost of qualifying property exceeds $2M	For the 2018-2022 tax years, business expense limitation increased to $5M, phased out when the cost of qualifying property exceeds $20M; also adds energy efficient heating and air-conditioning property as a qualified property	Increases maximum current expense threshold to $1M, phased out when the cost of qualifying property exceeds $2.5M; expands definition of qualified property to include all qualified improvement property and improvements to roofs, heating, ventilation, air-conditioning property, fire protection and alarm systems, and security systems made to nonresidential real property	Increases maximum current expense threshold to $1M, phased out when the cost of qualifying property exceeds $2.5M; expands definition of qualified property to include all qualified improvement property and improvements to roofs, heating, ventilation, air-conditioning property, fire protection and alarm systems, and security systems made to nonresidential real property

Business provisions in general				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
Use of the cash method of accounting	Farming businesses, qualified personal service corporations and C corporations with annual gross receipts that do not exceed $5M can generally use the cash method of accounting	Increase average gross receipt threshold to $25M, and extends cash method availability to certain farming entities; repeals requirement that the gross receipts threshold must be satisfied for all prior years	Increases annual gross receipts test to $15M, and extends to farming C corporations	Increase average gross receipt threshold to $25M, and extends cash method availability to certain farming entities; repeals requirement that the gross receipts threshold must be satisfied for all prior years
Accounting for inventories on accrual method	Generally, taxpayers with inventories must use accrual method of accounting; exception applies for taxpayers with average annual gross receipts under $1M and for taxpayers in certain industries with gross receipts less than $10M that are not otherwise prohibited from using the cash method	Increase average gross receipt threshold to $25M, and allow such taxpayers to treat inventories as nonincidental materials and supplies or follow their book method	Increase average gross receipt threshold to $15M; qualifying taxpayers may either use their book method or treat the inventories as nonincidental materials and supplies	Increase average gross receipt threshold to $25M, and allow such taxpayers to treat inventories as nonincidental materials and supplies or follow their book method
Accounting for UNICAP	Taxpayers who acquire property for resale and have $10M or less of annual gross receipts are not required to include additional section 263A costs in inventory (small taxpayers)	Expands exception for small taxpayers from UNICAP for gross receipts not exceeding $25M	Expands exception for small taxpayers from UNICAP for gross receipts not exceeding $15M	Expands exception for small taxpayers from UNICAP for gross receipts not exceeding $25M
Percentage-of-completion (PCM) method	Small construction contracts exempt from PCM; these include contracts for construction of real property expected to be completed within two years and the taxpayer's average gross receipts for the prior three years does not exceed $10M	Expands scope of small construction contracts to taxpayers with average gross receipts not exceeding $25M	Expands scope of small construction contracts to taxpayers with average gross receipts not exceeding $15M	Expands scope of small construction contracts to taxpayers with average gross receipts not exceeding $25M
Recovery periods for real property	Section 168(c) provides a recovery period of 27.5 and 39 years for residential rental property and nonresidential real property, respectively; separate definitions provided for qualified leasehold improvements, qualified restaurants, and qualified retail improvement property, which generally provide for a 15-year recovery period	No provision	Shortens recovery period for nonresidential real and residential rental property to 25 years; provides a general 10-year recovery period for qualified improvement property, and a 20-year ADS recovery period for such property; lowers the ADS recovery period to 30 years for residential rental property	Maintains the current MACRS recovery period of 39 and 27.5 years for nonresidential real and residential rental property; provides a general 15-year recovery period for qualified improvement property, and a 20-year ADS recovery period for such property; lowers the ADS recovery period to 30 years for residential rental property
Deferral of income	For accrual basis taxpayers, income is included in gross income when all events have occurred that fixes the right to receive such income and the amount can be determined with reasonable accuracy; Rev. Proc. 2004-34 provides a one-year deferral of certain advanced payments	No provision	All-events not met later than the tax year in which the item is taken into account as revenue in an applicable financial statement (exceptions for special methods of accounting); codifies the deferral method under Rev. Proc. 2004-34	All-events not met later than the tax year in which the item is taken into account as revenue in an applicable financial statement (exceptions for special methods of accounting); codifies the deferral method under Rev. Proc. 2004-34
Denial of certain deductions	Current code does not include a denial of a deduction for sexual harassment and abuse payments; generally considered ordinary business expenditures	No provision	No deduction for payments related to sexual harassment and sexual abuse and attorney's fees related to a settlement or payment subject to a nondisclosure agreement	No deduction for payments related to sexual harassment and sexual abuse and attorney's fees related to a settlement or payment subject to a nondisclosure agreement

Business provisions in general				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
Deductibility and reporting of fines and penalties	No deductions for bribe payments, health care fraud, lobbying payments, and any fines paid to the government for breaking the law	No provision	Fines or penalties paid or incurred to a government or governmental entity in relation to a violation of (or possible violation of) a law where the government is a complainant or investigator are not deductible; restitution exempted from nondeductibility; added reporting requirement detailing the fine or penalty to which section 162(f) applies	Fines or penalties paid or incurred to a government or governmental entity in relation to a violation of (or possible violation of) a law where the government is a complainant or investigator are not deductible; restitution exempted from nondeductibility; added reporting requirement detailing the fine or penalty to which section 162(f) applies
Self-created capital asset	Section 1221(a)(3) provides that capital assets include certain copyright, literary, musical, artistic composition, or similar property that was self-created	Excludes self-created patents, inventions, models or designs, or secret formulas or processes as qualifying as a capital asset under section 1221	No provision	Excludes self-created patents, inventions, models or designs, or secret formulas or processes from qualifying as a capital asset under section 1221
Sale or exchange of patents	Transfer of a substantial patent right shall be considered the sale or exchange of a capital asset held for more than one year	Repeals rule treating the sale or exchange of a patent as automatically resulting in a capital gain	No provision	No change in current law
Expensing costs of replanting citrus plants	No current provision	No provision	Allows certain minority co-owners of citrus plants that were lost or damaged due to a casualty event a current deduction for replanting costs; provision terminates 10 years after date of enactment	Allows certain minority co-owners of citrus plants that were lost or damaged due to a casualty event a current deduction for replanting costs; provision terminates 10 years after date of enactment
Interest capitalization	In general, interest capitalization applies to taxpayers who construct or produce tangible personal property that has a class life of 20 years or more, takes more than two years to complete, or takes more than one year to complete and production costs exceed $1M; production period includes aging period of goods	No provision	Excludes aging period of beer, wine, and distilled spirits from calculation of production period under UNICAP interest capitalization rules; provision does not apply to interest costs paid or accrued after Dec. 31, 2019	Excludes aging period of beer, wine, and distilled spirits from calculation of production period under UNICAP interest capitalization rules; provision does not apply to interest costs paid or accrued after Dec. 31, 2019
Local lobbying expenses	Section 162(e) allows a deduction for lobbying and political expenditures in the case of any legislation of any local counsel, which includes Indian tribal governments	Eliminate the deduction for local lobbying expenses	Eliminate the deduction for local lobbying expenses	Eliminate the deduction for local lobbying expenses for amounts paid or incurred after the date of enactment
Recovery period for farming property	Section 168(b)(2)(B) provides that property used in a farming business must use the 150% declining balance method	No provision	Repeals the requirement that property used in the farming business use the 150% declining balance method	Repeals the requirement that property used in the farming business use the 150% declining balance method

Business provisions in general				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
Tax gain on the sale of a partnership interest on lookthrough basis	Rev. Rul. 91-32 provides that in determining the source of gain or loss from the sale or exchange of an interest in a foreign partnership, if there is unrealized gain or loss in partnership assets that would be treated as effectively connected with the conduct of a US trade or business if those assets were sold by the partnership, then some or all of a 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 US trade or business The Tax Court recently declined to follow Rev. Rul. 91-32 in *Grecian Magnesite Mining, Indus. & Shipping Co. v. Commissioner,* 149 T.C. No. 3 (July 13, 2017)	No provision	Codifies IRS position in Rev. Rul. 91-32 by treating foreign person's gain from the sale or exchange of partnership interest as effectively connected income (ECI) to the extent the foreign person would have recognized ECI had the partnership sold all of its assets for their fair market value as of the date of the foreign person's sale or exchange Also requires the transferee of a partnership interest to withhold 10% of the amount realized on the sale or exchange of a partnership interest unless the transferor certifies that the transferor is not a nonresident alien individual or foreign corporation The provision (including withholding requirement) applies to sales, exchanges, and dispositions on or after Nov. 27, 2017	Codifies the IRS's position in Rev. Rul. 91-32 by treating a foreign person's gain from the sale or exchange of a partnership interest as effectively connected income (ECI) to the extent the foreign person would have recognized ECI had the partnership sold all of its assets for their fair market value as of the date of the foreign person's sale or exchange The provision also requires the transferee of a partnership interest to withhold 10% of the amount realized on the sale or exchange of a partnership interest unless the transferor certifies that the transferor is not a nonresident alien individual or foreign corporation The portion of the provision treating gain or loss on sale of a partnership interest as ECI is effective for sales, exchanges, and dispositions on or after Nov. 27, 2017, and the portion of the provision requiring withholding on sales or exchanges of partnership interests is effective for sales, exchanges, and dispositions after Dec. 31, 2017
Technical terminations of partnerships	Section 708(b)(1)(B) provides that a partnership terminates if within a 12-month period there is a sale or exchange of 50% or more of the total interests in partnership capital and profits	Repeals the technical termination rule for partnerships; thus, a partnership would be treated as continuing even if 50% or more of the total capital and profits interests of the partnership are sold or exchanged, and new elections would not be required or permitted	No provision	Repeals the technical termination rule for partnerships; thus, a partnership would be treated as continuing even if 50% or more of the total capital and profits interests of the partnership are sold or exchanged, and new elections would not be required or permitted

Business credit provisions

Business credit provisions				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
Production tax credit (PTC)	Income tax credit is allowed under section 45 for production of electricity from qualified energy resources at qualified facilities Credit rate, initially set at 1.5 cents per kilowatt-hour (reduced by one-half for certain renewable resources) is adjusted annually for inflation To qualify for the credit, a wind facility must begin construction before Jan. 1, 2020; however, credit amount phases down 20% each year beginning in 2017 To qualify, facilities that produce electricity from other resources (e.g., biomass, trash, geothermal, hydropower) must have begun construction before Jan. 1, 2017	Reduce value of PTC to original 1992 rate of 1.5 cents per kilowatt-hour by eliminating inflation index (current PTC rate is 2.4 cents per kilowatt-hour) Reduction in value applicable only to electricity produced from projects that begin construction after date of enactment and would be in addition to PTC phaseout implemented in 2015; would not impact refined coal projects No change to current-law schedule for sunsetting PTC for electricity produced from wind projects constructed after 2019 Introduces potentially significant “continuous program of construction” condition that must be satisfied to preserve benefits of begun-construction status (safe harbors in current IRS guidance protect taxpayers from having to satisfy continuous construction condition) This condition applies retroactively, could disrupt projects already underway, and make it more difficult for projects to qualify for marginally greater PTC benefits; Ways & Means explanation clarifies that provision was intended to codify current IRS begun construction rules	No proposed change in law; phaseout of the PTC continues as originally enacted in 2015	No proposed change in law; phaseout of the PTC continues as originally enacted in 2015
Investment tax credit (ITC)	Section 48 commercial ITC provides a tax credit for investments in solar energy property Credit amount is 30% for property that begins construction before Jan. 1, 2020 and is placed into service by Dec. 31, 2023 Credit phases down to 26% in 2020, 22% in 2021, 18% in 2022, and drops to a permanent 10% credit for all other property	ITC phasedown remains consistent with current law, but 10% ITC is eliminated entirely for projects that begin construction after 2027 Introduces potentially significant “continuous program of construction” condition that must be satisfied to preserve benefits of begun-construction status Forthcoming IRS guidance expected to be similar to guidance for the PTC; Ways & Means Committee Explanation of the provision for PTC clarifies that provision was intended to codify current IRS begun construction rules	No proposed change in law; phasedown of ITC from 30% to 10% continues as originally enacted in 2015	No proposed change in law; phasedown of ITC from 30% to 10% continues as originally enacted in 2015

Business credit provisions				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
Orphaned ITC credits	Section 48 commercial ITC for qualified microturbines, fuel cells, combined heat and power systems, and geothermal energy property were not extended in 2015 and expired for property placed in service after Dec. 31, 2016	Restores so-called "orphaned" credits Fiber-optic solar energy, qualified fuel cell, and qualified small wind energy property eligible for 30% ITC if construction begins before 2020 and would be phased out for construction that begins before 2022 using the same schedule currently applicable to solar energy property Qualified microturbine, combined heat and power systems, and geothermal energy property eligible for 10% ITC if construction begins before 2022	No proposed change in law (no extension of the other energy tax credits left out of the 2015 extenders legislation) Senate purportedly preparing separate extenders bill expected to include these "orphaned" credits and follow the same phaseout schedule as House bill	No proposed change in law (no extension of the other energy tax credits left out of the 2015 extenders legislation) Senate purportedly preparing separate extenders bill expected to include these "orphaned" credits and follow the same phaseout schedule as House bill
Orphaned residential ITC credits	Section 25D residential energy-efficient property credit provides an investment credit based on qualified expenditures; credit was extended in 2015 for certain solar property expenditures, but expired for expenditures related to geothermal, small wind and fuel cell property placed in service after Dec. 31, 2016	Extends section 25D credit for residential energy-efficient property for all qualified solar, geothermal, small wind and fuel cell property placed in service prior to 2022, subject to a reduced rate of 26% for property placed in service during 2020 and 22% for property placed in service during 2021; effective for property placed in service after Dec. 31, 2016 Harmonizes and extends residential ITC to also include those orphaned technologies (small wind, fuel cells, etc.) that were not included in the 2015 extension	No proposed change in law: existing rules stay in place with only solar electric expenditures qualifying for phaseout of section 25D residential ITC for property installed before Jan. 1, 2022 Senate preparing separate extenders bill expected to include these "orphaned" credits and follow the same phaseout schedule as House bill	No proposed change in law: existing rules stay in place with only solar electric expenditures qualifying for phaseout of section 25D residential ITC for property installed before Jan. 1, 2022 Senate preparing separate extenders bill expected to include these "orphaned" credits and follow the same phaseout schedule as House bill
Plug-in electric vehicle credit	Section 30D provides a tax credit for certain qualified plug-in electric vehicles	Repeals credit for new qualified plug-in electric drive motor vehicles, effective for vehicles placed in service in taxable years beginning after Dec. 31, 2017	No proposed change in law; existing rules stay in place	No proposed change in law; existing rules stay in place
New markets credits (NMTC)	Credit under section 45D for qualified equity investments made to acquire stock in a corporation, or a capital interest in a partnership, that is a qualified community development entity (CDE) Credit amount allowable to investor (either the original purchaser or a subsequent holder) is (1) a 5% credit for the year in which the equity interest is purchased from the CDE and for each of the following two years, and (2) a 6% credit for each of the following four years	No additional NMTCs allocated after calendar 2017 (current NMTC allocation round expected to be awarded in early 2018) Credits that have already been allocated including calendar 2017 allocation may be used over the course of up to seven years as contemplated in credit's multiyear timeline	No proposed change in law Additional tax credit allocations to be made for calendar 2017, 2018, and 2019, with credit phased out after 2019 New Opportunity Zone provision would be established consolidating current tax law provisions similar to the former Enterprise Zones for the purpose of encouraging private investment in distressed communities	No proposed change in law Additional tax credit allocations to be made for calendar 2017, 2018, and 2019, with credit phased out after 2019 Certain administrative changes were made to the new Opportunity Zone Credit provision that would be established consolidating current tax law provisions similar to the former Enterprise Zones for the purpose of encouraging private investment in distressed communities

Business credit provisions				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
Low-income housing credit (LIHTC)	Section 42 credits may be claimed over 10-year period for cost of building rental housing occupied by tenants with incomes below specified levels; credit amount for any taxable year in the credit period is the applicable percentage of the qualified basis of each qualified low-income building	Retains credit but eliminates issuance of tax-exempt private activity bonds, including those used to finance construction of multifamily homes (i.e., Multifamily Housing Bonds, which are directly responsible for more than 50% of the affordable rental units produced each year under the LIHTC program) 4% credit is currently coupled with Multifamily Housing Bonds, which in turn are allocated based on a state's volume cap for private activity bonds Expected to significantly reduce the size of LIHTC tax equity market if enacted	Retains LIHTC with modifications Adds veterans to the existing law exception to the general public use requirement, enabling developers to target their LIHTC developments to veterans Automatically provides a 25% basis boost to 9% LIHTC developments located in rural areas as defined under section 520 of the Housing Act of 1949 For such rural properties, it would remove current-law discretion that state agencies have on providing 30% basis boost	No proposed change in law; existing rules stay in place
Historic rehabilitation tax credit	20% credit for qualified rehabilitation expenditures with respect to a certified historic structure in section 47	Repeals 10% credit for pre-1936 buildings, and 20% credit for certified historic structures effective for qualified rehabilitation expenditures paid or incurred after Dec. 31, 2017 Transition rule provides that in the case of qualified rehabilitation expenditures (for either a certified historic structure or a pre-1936 building), with respect to any building owned or leased by the taxpayer at all times on and after Jan. 1, 2018, the 24-month period selected by the taxpayer (under section 47(c)(1)(C)) is to begin not later than the end of the 180-day period beginning on the date of enactment	Repeals the 10% credit for pre-1936 buildings Modifies the 20% credit for certified historic structures, generally for amounts paid or incurred after 2017; credit amount remains at 20%, but is claimed ratably over a five-year period beginning in the tax year in which a qualified structure is placed in service Both provisions effective for qualified rehabilitation expenditures paid or incurred after Dec. 31, 2017 Includes same 2-year transition rule as the House bill	Follows Senate amendment but modifies the transition rule under the effective date relating to qualified rehabilitation expenditures under certain phased rehabilitations for which the taxpayer may select a 60-month period Applies to amounts paid or incurred after Dec. 31, 2017 Transition rule provides that in the case of qualified rehabilitation expenditures (for either a certified historic structure or a pre-1936 building), with respect to any building owned or leased (as provided under present law) by the taxpayer at all times on and after Jan. 1, 2018, the 24-month period selected by the taxpayer (section 47(c)(1)(C)(i)), or the 60-month period selected by the taxpayer under the rule for phased rehabilitation (section 47(c)(1)(C)(ii)), is to begin not later than the end of the 180-day period beginning on the date of enactment, and the amendments made by the provision apply to such expenditures paid or incurred after the end of the taxable year in which such 24-month or 60-month period ends
Work Opportunity Tax Credit (WOTC)	Section 51 provides that an employer may claim a credit of up to 40% of qualified first-year wages of employees belonging to certain target groups	Repeals the WOTC for amounts paid or incurred to individuals who begin work for the employer after Dec. 31, 2017	No proposed change in law; existing rules stay in place with credit allowed through 2019	No proposed change in law; existing rules stay in place with credit allowed through 2019

Business credit provisions				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
PTC for qualifying advanced nuclear facilities	Taxpayers producing electricity at a qualifying advanced nuclear power facility may claim a credit equal to 1.8 cents per kilowatt-hour of electricity produced for the eight-year period starting when the facility is placed in service as provided by section 45J	Beginning after Jan. 1, 2021, the Secretary shall reallocate any national megawatt capacity that remains unused under the cap, first to qualifying facilities to the extent such facilities do not receive an allocation equal to their full capacity, and then to facilities placed in service after such date New credit transfer provision with respect to certain public utilities would make certain public entities eligible for an election to transfer advanced nuclear production tax credits to specified project participants Effective for tax years beginning after date of enactment	No proposed change in law; existing rules stay in place effectively repealing the credit since current projects under construction are not thought to be able to meet statutory deadlines Senate preparing separate extenders bill expected to include the same modifications as proposed in the House bill	No proposed change in law: existing rules stay in place effectively repealing the credit since current projects under construction are not thought to be able to meet statutory deadlines Senate preparing separate extenders bill expected to include the same modifications as proposed in the House bill
Enhanced oil recovery credit	Section 43 provides a 15% credit for expenses associated with an enhanced oil recovery (EOR) project Qualified EOR costs consist of the following designated expenses associated with an EOR project: (1) amounts paid for depreciable tangible property; (2) intangible drilling and development expenses; (3) tertiary injectant expenses; and (4) construction costs for certain Alaskan natural gas treatment facilities	Repeal effective for tax years beginning after Dec. 31, 2017	No proposed change in law: existing rules stay in place	No proposed change in law; existing rules stay in place
Marginal well credit	Section 45I provides a $3-per-barrel credit for production of crude oil and a $0.50 credit per 1,000 cubic feet of qualified natural gas production	Repeal effective for tax years beginning after Dec. 31, 2017	No proposed change in law; existing rules stay in place	No proposed change in law; existing rules stay in place

Business credit provisions				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
Orphan drug credit	Section 45C provides 50% business tax credit for qualified clinical testing expenses incurred in testing of certain drugs for rare diseases or conditions Qualified clinical testing expenses are costs incurred to test an orphan drug after the drug has been approved for human testing by the Food and Drug Administration (FDA) but before the drug has been approved for sale by the FDA	Repeal effective for drug manufacturers who incur qualified clinical testing expenses in tax years beginning after Dec. 31, 2017	Limits credit to 50% of so much of qualified clinical testing expenses for the taxable year as exceeds 50% of average qualified clinical testing expenses for the three taxable years preceding taxable year for which the credit is being determined If there are no qualified clinical expenses during at least one of the three preceding taxable years, credit is equal to 25% of qualified expenses Aggregation and other special rules similar to those applicable to the research credit apply where there are controlled groups of corporations, estates, and trusts claiming the credit, mergers and acquisitions of taxpayers, and short taxable years Taxpayers may elect a reduced credit in lieu of reducing otherwise allowable deductions in a manner similar to the research credit under section 280C Qualified clinical testing expenses limited to the extent the testing giving rise to such expenses is related to the use of a drug which has previously been approved under section 505 of the Federal Food, Drug, and Cosmetic Act for use in the treatment of any other disease or condition, if all such diseases or conditions in the aggregate (including the rare disease or condition with respect to which the credit is otherwise being determined) affect more than 200,000 persons in the United States Effective for amounts paid or incurred in taxable years beginning after Dec. 31, 2017	Follows the Senate bill, but reduces the credit rate to 25% of qualified clinical testing expenses

Business credit provisions				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
FICA tip credit	Certain food or beverage establishments may elect to claim a business tax credit equal to an employer's taxes under the Federal Insurance Contributions Act (FICA) paid on tips in excess of those treated as wages for purposes of meeting the minimum wage requirements of the Fair Labor Standards Act (FLSA) as in effect on Jan. 1, 2007 under section 45B Applies only with respect to FICA taxes paid on tips received from customers in connection with providing, delivering, or serving of food or beverages for consumption if the tipping of employees delivering or serving food or beverages by customers is customary	Modifies FICA tip credit to reflect the current minimum wage, and adds a reporting requirement for all restaurants claiming the credit for the portion of employer social security taxes paid with respect to employee cash tips Effective for tips received for services performed after Dec. 31, 2017	No proposed change in law: existing rules stay in place	No proposed change in law; existing rules stay in place
Employer-provided childcare credit	Taxpayers eligible for a tax credit equal to 25% of qualified expenditures for employee childcare and 10% of qualified expenditures for childcare resource and referral services; maximum total credit that may be claimed by a taxpayer may not exceed $150K per taxable year Credit is part of the general business credit	Repeal effective for tax years beginning after Dec. 31, 2017	No proposed change in law: existing rules stay in place	No proposed change in law; existing rules stay in place
Access to disabled individuals credit	Section 44 provides a 50% credit for eligible access expenditures paid or incurred by an eligible small business for the taxable year; limited to eligible access expenditures exceeding $250 but not exceeding $10.5K Credit is part of the general business credit	Repeal effective for tax years beginning after Dec. 31, 2017	No proposed change in law: existing rules stay in place	No proposed change in law; existing rules stay in place

Business credit provisions				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
Employer credit for paid family and medical leave	No provision	No provision	New section 45S would permit eligible employers (employers that allow all qualifying full-time employees at least two weeks annual paid family and medical leave and allow part-time employees a commensurate amount of leave on a pro rata basis) to claim a business credit for 12.5% of the wages paid to qualifying employees during any period in which such employees are on family and medical leave if the payment rate under the program is 50% of the wages normally paid to an employee Credit would be increased by 0.25 percentage points (but not above 25%) for each percentage point by which the rate of payment exceeds 50% Effective for wages paid in tax years beginning after Dec. 31, 2017; would not apply to wages paid in tax years beginning after Dec. 31, 2019	Follows Senate bill
Federal credit impact of Base Erosion and Anti-Abuse Tax (BEAT)	No provision	No provision	For multinational companies covered under the BEAT provisions, general business tax credits would, as drafted, be subject to a reduction in value (R&D credits would be exempt through 2025) BEAT provision may also significantly impact major financial institutions from the ability to participate in the tax equity financing marketplace BEAT would be applicable to credits generated as a result of projects that began operating in prior years	Follows the Senate bill with modifications; the rates of the BEAT are modified and 80% of a taxpayer's certain general business credits (renewable electricity production tax credit, energy investment tax credit and low-income housing tax credit) may be used against the BEAT

International provisions

International provisions				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
Regime type	Worldwide regime with deferral and foreign tax credit offsets; applies to corporations and individuals	Participation exemption regime with 100% dividends received deduction; only available to corporations	Participation exemption regime with 100% dividends received deduction; only available to corporations	Participation exemption regime with 100% dividends received deduction (only available to corporations)
Foreign-held earnings and profits	US tax deferred until income is repatriated	Deemed repatriation of previously untaxed E&P at rate of 7% (noncash) or 14% (cash and equivalents) • Applied to E&P as of Nov. 2, 2017 or Dec. 31, 2017, whichever is higher • Payable over 8 years	Deemed repatriation of previously untaxed E&P at rate of 7.49% (noncash) or 14.49% (cash and equivalents) • Clawback of rate reduction if company inverts within 10 years after bill enactment • Payable over 8 years	Deemed repatriation of previously untaxed E&P at rate of 8% (noncash) or 15.5% (cash and equivalents) • Clawback of rate reduction if company inverts within 10 years after bill enactment • Payable over 8 years
Intangible property	No provision	No provision	20% tax on foreign-derived intangible income (FDII) with 37.5% deduction through 2025, then 21.875% Opens path to tax-free repatriation of IP	20% tax on foreign-derived intangible income (FDII) with 37.5% deduction through 2025, then 21.875%
Base-erosion prevention measures	Subpart F rules limit deferral for certain types of passive and mobile income	20% tax on 50% of foreign high return amounts	20% tax on "global intangible low-taxed income" (GILTI) with 50% deduction through 2025, then 37.5%	20% tax on GILTI with 50% deduction through 2025, then 37.5%
		Additional limits on deductions by US corporations of interest paid on debt	Additional limits on deductions by US corporations of interest paid on debt	No provision
		Tax of up to 20% on payments made to related parties abroad from US operations unless treated as "effectively connected income" (ECI)	10% "minimum tax" on taxable income in excess of deductible payments to related foreign parties Deduction denied for interest or royalties paid on certain hybrid transactions if no corresponding inclusion to related party or if related party is allowed deduction	10% "minimum tax" on taxable income in excess of deductible payments to related foreign parties Deduction denied for interest or royalties paid on certain hybrid transactions if no corresponding inclusion to related party or if related party is allowed deduction

Insurance provisions

Insurance provisions				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
Surtax on certain life insurance company income	No provision	Impose 8% surtax based on taxable life insurance company income (in addition to the corporate tax rate), effective for taxable years beginning after Dec. 31, 2017	No provision	No provision
Company share of DRD and tax-exempt interest	Company share is calculated based on a complicated formula which differs for general and separate accounts but is generally 100% less the ratio of required interest (or amounts retained) over investment income	No provision	Modify life insurance proration rules for the DRD within 805(a)(4) Define "company share" as a flat 70% and define the "policyholder share" as 30% for purposes of DRD and tax-exempt interest Effective for taxable years beginning after Dec. 31, 2017	Follows Senate bill
Capitalization of DAC	Deferred acquisition costs (DAC) applicable to specified insurance contracts under IRC section 848 Capitalization rates based on net premiums: • Annuity contracts—1.75% • Group contracts—2.05% • All other contracts—7.7% Amortization period is 10 years	No provision	Increase capitalization rates (DAC) applicable to specified insurance contracts under section 848 • Annuity contracts—2.1% • Group contracts—2.46% • All other contracts—9.24% Increase amortization period to 15 years Effective for taxable years beginning after Dec. 31, 2017	Generally follows Senate bill with slight reductions to capitalization rates (likely due to slightly increased corporate tax rate in conference agreement over what was proposed in the House and Senate bills) 15-year amortization period Capitalization rates • Annuity contracts—2.09% • Group contracts—2.45% • All other contracts—9.2% Transition rule allows capitalized DAC amounts as of Dec. 31, 2017, to continue 10-year amortization
Computation of life insurance tax reserves	Reserves are computed based on an interest rate equal to the greater of the applicable federal interest rate or the prevailing state assumed interest rate	No provision	Eliminate federally prescribed reserve computation of life insurance reserves for tax purposes Base tax reserves on greater of net surrender value of the contract or a flat 92.87% of statutory reserves Separate account reserves would continue to be accounted as under current law Effective for taxable years beginning after Dec. 31, 2017	Follows Senate bill with modifications • Base tax reserves on greater of net surrender value of contract or flat 92.81% of statutory reserves • Reserve reporting requirement to be implemented • Effective for taxable years beginning after Dec. 31, 2017 • Eight-year spread of reserves difference under old and new methods
Adjustment for change in computing reserves	Income or expense resulting from a change in method of computing reserves is spread over 10 years beginning in the year following the change	Repeal section 807(f) 10-year spread for 807(f) adjustments Subject to normal change in method of accounting rules Does not require a request for change in method of accounting Effective for losses arising in taxable years beginning after Dec. 31, 2017	Follows House bill	Follows House and Senate bills; presumably no change in spread for existing 807(f) amounts, but not addressed in bill text

Insurance provisions				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
Net operating losses of life insurance companies	Life companies allowed a 3-year carryback and 15-year carryover	Life insurance companies follow general section 172 rules Change operations loss carryover and carryback period through modification of section 172: operations losses no longer eligible for carryback but may be carried forward indefinitely Retain the special 2-year back, 20-year forward carryback and carryover rule for nonlife insurance companies by amending section 172, and exempt nonlife insurance companies from 80% limitation on use of NOLs Effective for losses arising in taxable years beginning after Dec. 31, 2017	Follows House bill	Follows House and Senate bills General corporate NOL provision in the agreed bill, which would now apply to life insurance companies, allows NOL carryforwards to offset only 80% of taxable income
Small life insurance company deduction	Life insurance companies may deduct 60% of their first $3M of life insurance-related income; deduction is phased out for companies with income between $3M and $15M, and is not available to life insurance companies with assets of at least $500M	Repeal small life insurance company deduction in current section 806 and make corresponding revisions to sections 453B(e) and 953(b), effective for taxable years beginning after Dec. 31, 2017	Follows House bill	Follows House and Senate bills
Repeal of special estimated tax payments	Section 847 provides that insurance companies that elect to claim a deduction equal to the difference between the amount of reserves computed on a discounted basis and the amount computed on an undiscounted basis are required to make a special estimated tax payment equal to the tax benefit attributable to the deduction	Repeal section 847 for taxable years beginning after Dec. 31, 2017	Follows House bill but adds transition rules	Follows House and Senate bills, with income and deductions all taken into account for 2018 taxable year; any excess tax payments are to be treated as payment under section 6655
Modifications to proration rules for P&C companies	Reduce DRD and tax-exempt interest by a flat 15%	Modifications include replacing the fixed 15% reduction in the reserve deduction for P&C companies with 26.25% rate, effective for taxable years beginning after Dec. 31, 2017	Ties the proration rate to the corporate tax rate for taxable years beginning after Dec. 31, 2017	Follows Senate bill; new proration percentage is 5.25% divided by top corporate tax rate, i.e., 25% for 2018
Repeal special rule for distributions from policyholders surplus accounts (PSAs)	Section 815 prescribes rules regarding taxation of certain distributions from PSAs	Repeal current section 815; any remaining balance of the PSA would be included in income over eight years for taxable years beginning after Dec. 31, 2017	Follows House bill	Follows House and Senate bills; eight-year transition rule for income inclusions

Insurance provisions				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
Discounting rules for P&C insurance companies	Discount reserves based on the 60-month rolling average AFIR	Require P&C insurance companies to use higher interest rate for section 846 purposes • Use corporate bond yield curve to discount unpaid losses • 18- or 25-year limitation for special rule extending loss payment patterns for certain lines of business Repeal section 846(e) election to use company-specific historical loss payment patterns Effective for taxable years beginning after Dec. 31, 2017	No provision	Generally follows House bill Corporate bond yield curve for preceding 60-month period on investment grade corporate bonds with varying maturities and that are in top three quality levels available Present-law 10-year period for certain long tail lines of business is extended for maximum of 24 more years (instead of 15 years) Repeals section 846(e) election that permits taxpayer to use its own payment pattern Effective for taxable years beginning after Dec. 31, 2017 Transition rule provides that for first taxable year beginning in 2018, amount of unpaid losses and expenses at the end of the preceding taxable year is determined as if the provision had applied to these items in such preceding taxable year; any adjustment spread over eight taxable years beginning in 2018
Net operating loss for nonlife insurance companies	Nonlife insurance companies follow the same rules as general corporations: losses may be carried back 2 years and forward 20	Change to corporate NOL rules would apply to nonlife insurance companies: no carryback and indefinite carryforward	Change to corporate NOL rules provides an exception to nonlife insurance companies: current-law carryback and carryforward rules remain unchanged (back 2 and forward 20)	Follows Senate bill; 80% limitation on NOL use does not apply to nonlife insurance companies
Health care or health insurance provisions	Individual mandate enacted in the Patient Protection and Affordable Care Act of 2010 requires a penalty to the extent minimum essential coverage is not maintained	No provision	Reduces penalty to zero	Follows Senate bill; effective date is Jan. 1, 2019
Life insurance product taxation	No reporting requirements on life settlement transactions Lack of clarity regarding basis in life insurance contracts Exceptions exist to transfer for value which ordinarily would disallow the exclusion of death benefits from taxable income	No provision	New reporting requirements on sale of existing life insurance policies (taxable years beginning after Dec. 31, 2017) Basis in contract not reduced by cost of insurance (transactions entered into after Dec. 31, 2017) Transfer for value exception narrowed (transactions entered into after Dec. 31, 2017)	Reporting provision follows Senate bill for reportable policy sales and death proceeds on or after Dec. 31, 2017 Basis clarification follows Senate bill, effective for policy transactions entered into on or after Aug. 25, 2009 (retroactive) Transfer for value exception follows Senate bill for transactions entered into after Dec. 31, 2017

Individual provisions

Individual provisions				
Provision	**2017 law/Scheduled 2018 phase-ins**	**House bill**	**Senate bill**	**Enacted legislation**
Income tax rate structure	7 brackets; income thresholds indexed for CPI Top rate of 39.6% on income >$426.7K/$480.05K (single/joint)	4 brackets; income thresholds indexed for chained CPI Top rate of 39.6% on income >$500K/$1M 6% bubble tax on income $1M–$1.2M	7 brackets; income thresholds indexed for chained CPI Top rate of 38.5% on income >$500K/$1M Changes sunset Dec. 31, 2025	7 brackets; income thresholds indexed for chained CPI Top rate of 37% on income >$500K/$600K Changes sunset Dec. 31, 2025
Net investment income and Medicare tax on earned income	Additional 3.8% on net investment income >$125K/$250K MAGI Additional 0.9% Medicare tax on income >$200K/$250K	No change	No change	No change
Standard deduction	$6.5K/$13K	$12K/$24K	$12K/$24K Sunsets Dec. 31, 2025	Follows Senate bill
Personal exemption	$4.15K exemption for each member of household, phased out for higher AGIs	Repealed	Repealed through Dec. 31, 2025	Follows Senate bill
Limitation on itemized deductions	Pease limitation for AGI > $266.7K/$320K	Repealed	Repealed through Dec. 31, 2025	Follows Senate bill
Child tax credit and family tax credit	$1K credit per child under age 17; phaseout for AGI >$75K/$110K	$1.6K credit per child under age 17 or $300 per nonchild dependent; new $300 credit for each filer • $300 credits nonrefundable and sunset Dec. 31, 2022 • Phaseout increased to $115K/$230K • SSN required for entire credit	$2K credit per child under age 18 and $500 per nonchild dependent; no family credit • Changes sunset Dec. 31, 2025 • Phaseout increased to $500K • SSN required for refundable portion of credit	$2K credit per child under age 17 and $500 per nonchild dependent; no family credit • Changes sunset Dec. 31, 2025 • Phaseout increased to $400K (joint) • Maximum refundable credit of $1.4K per qualifying child; credit for nonchild dependent is nonrefundable • SSN required for refundable portion of credit
AMT	26%/28% on alternative minimum taxable income	Repealed: 50% of AMT credit carryforwards refundable in 2019–2021; remaining credits refundable from 2022	Exemption increased through Dec. 31, 2025	Retained; exemption increases to $70.3K/$109.4K; phaseout thresholds increased to $500K/$1M; indexed for inflation; sunsets Dec. 31, 2025
State and local tax (SALT) and property tax deduction	State and local income and property taxes or sales taxes fully deductible	Property taxes up to $10K deductible; other SALT generally nondeductible • Deduction still allowed for taxes accrued in business • $10K not inflation indexed	Property taxes up to $10K deductible; other SALT generally nondeductible; sunsets Dec. 31, 2025 • Deduction still allowed for taxes accrued in business • $10K not inflation indexed • Sunsets after Dec. 31, 2025	Deduction of up to $10K ($5K MFS) for the aggregate of nonbusiness (1) state and local property taxes, and (2) state and local income taxes or sales taxes; no deduction for foreign nonbusiness property taxes; sunsets Dec. 31, 2025 Prepayments of state and local income tax for 2018 made in 2017 are treated as paid as of last day of 2018

Individual provisions				
Provision	**2017 law/Scheduled 2018 phase-ins**	**House bill**	**Senate bill**	**Enacted legislation**
Mortgage interest deduction	Deduction on first $1M of debt used to secure primary or secondary residence, and first $100K of home equity debt	Interest deductible on first $500K of debt for primary residence only • Effective for debt incurred after Nov. 2, 2017	2017-law deduction for primary/secondary residence retained • Home equity debt deduction repealed through Dec. 31, 2025	Interest deductible on first $750K ($375K married filing separate) of acquisition indebtedness on primary and secondary residences; sunsets Dec. 31, 2025 • Effective for debt incurred after Dec. 15, 2017 • Existing mortgages grandfathered • Home equity debt deduction repealed through Dec. 31, 2025
Exclusion of gain from sale of principal residence	Up to $250K/$500K of gain on sale excluded from gross income; must have been principal residence 2 of past 5 years; allowed once every 2 years	Residency required 5 of past 8 years; exclusion allowed once every 5 years; if average MAGI for the taxable year and the 2 preceding taxable years exceeds $250K/$500K, the amount excluded from gross income is reduced by the amount of such excess	Residency required 5 of past 8 years; exclusion allowed once every 5 years through Dec. 31, 2025	No provision (retains current law)
Individual health insurance mandate (Affordable Care Act)	Those who fail to maintain health coverage owe penalty of 2.5% of AGI, or $695 per adult/$347.50 per child in 2017	No provision	Penalty lowered to zero after Dec. 31, 2018	Penalty lowered to zero after Dec. 31, 2018
Carried interest	May qualify for long-term capital gain treatment under general rules	Increases the holding period requirement under section 1222 from 1 year to 3 years for long-term capital gain with respect to certain partnership interests transferred to or held by the taxpayer in connection with the performance of services	Follows House bill	Follows House bill
Unreimbursed medical expenses	Deductible subject to various AGI limits	Repealed	Deductible subject to 7.5% of AGI limitation for 2018 and 2019; percentage increases to 10% in 2020	Deductible subject to 7.5% of AGI limitation for 2017 and 2018; percentage increases to 10% in 2019
Tax preparation services deduction	Allowed as a 2% miscellaneous itemized deduction	Repealed	Repealed through Dec. 31, 2025	Follows Senate bill
Miscellaneous itemized deductions —2% floor	Certain deductions (ex. investment/advisor fees) allowed subject to a 2% of AGI floor	No provision	Repealed through Dec. 31, 2025 Note: Under this provision, the Senate version appears to preclude a deduction for all administrative expenses for trusts and estates	Follows Senate bill
Charitable contributions	Deductible subject to various AGI limits	Increased limitation for cash contributions from 50% to 60%; all other AGI limits remain unchanged; deduction denied for payments made in exchange for college athletic event seating rights	Increased limitation for cash contributions from 50% to 60%; all other AGI limits remain unchanged; sunsets Dec. 31, 2025	Increased limitation for cash contributions from 50% to 60%; sunsets Dec. 31, 2025; all other AGI limits remain unchanged; deduction denied for payments made in exchange for college athletic event seating rights
All personal casualty losses	Deductible subject to 10% of AGI	Repealed except for losses in federally declared disaster areas	Repealed except for losses in federally declared disaster areas through Dec. 31, 2025	Follows Senate bill

Individual provisions				
Provision	**2017 law/Scheduled 2018 phase-ins**	**House bill**	**Senate bill**	**Enacted legislation**
Excess business loss limitation	A limitation on excess farm losses applies to individuals	No provision	Expands limitation under current law to apply to excess business losses of a taxpayer • Excess business loss is the excess of aggregate business deductions over sum of aggregate business income plus threshold amount ($250K/$500K) • Carried forward as part of individual NOL • Applies at partner or S corporation shareholder level for pass-through businesses • Effective for taxable years beginning after Dec. 31, 2017; sunsets after Dec. 31, 2025	Follows Senate bill
Net operating loss deduction	2-year carryback and 20-year carryforward allowed to offset taxable income	NOL use limited to 90% of taxable income; carryforward period made indefinite; NOLs increased by interest factor; carrybacks not allowed	Limited to 90% of taxable income through 2022, then 80%; carryforward period made indefinite; carrybacks not allowed	Limited to the lesser of 80% of taxable income (excluding NOLs) or the aggregate NOL carryforward/carryback for tax years beginning after Dec. 31, 2017; carryforward period made indefinite; carrybacks not allowed
Cost basis of specified securities	Unless the average basis method is permitted, a taxpayer who sells stock that the taxpayer acquired on different dates or at different prices and who does not adequately identify the lot from which the stock is sold, must treat the stock sold on a first-in first-out basis to determine the basis and holding period	No provision	Cost basis of securities sold determined on a first-in first-out basis except to the extent the average basis method is otherwise allowed	No provision
Student loan interest deduction	An individual may claim an above-the-line deduction for interest payments on qualified education loans for qualified higher education expenses. The maximum amount of the deduction is $2.5K	Repealed	No provision	No provision
Alimony	Alimony payments are deductible by the payer and taxable to the payee	Alimony payments not deductible to the payer and not taxable to the payee. Applies to divorce or separation agreements executed after Dec. 31, 2017 or modified after Dec. 31, 2017 to apply these law changes	No provision	Alimony payments not deductible to the payer and not taxable to the payee. Applies to divorce or separation agreements executed after Dec. 31, 2018 or modified after Dec. 31, 2018 to apply these law changes
Unreimbursed employee expenses: Moving expenses	Deductible subject to 2% AGI limitation	Repealed, except for active duty armed forces members moving pursuant to military orders; effective for taxable years beginning after Dec. 31, 2017	Repealed for taxable years 2018 through 2025 with an exception for armed forces members moving pursuant to military orders	Follows Senate bill
Estate tax, generation-skipping tax, and gift tax	40% estate and generation-skipping tax; basic exclusion amount of $5M per taxpayer, adjusted for inflation ($5.6M in 2018)	40% estate and generation-skipping tax through 2023; both repealed in 2024; gift tax lowered to 35%; basic exclusion amount increased to $10M per taxpayer, adjusted for inflation	40% estate, gift and generation-skipping tax; basic exclusion amount of $10M per taxpayer, adjusted for inflation; increased exemption sunsets Dec. 31, 2025	Follows Senate bill (as adjusted for inflation, this equals $11.2M per taxpayer in 2018); increased exemption sunsets Dec. 31, 2025

Compensation and benefits provisions

Compensation and benefits provisions				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
Entertainment, etc., expenses	50% deduction for qualified expenses	Deduction disallowed; no deduction for transportation fringe benefits, athletic facilities, or personal amenities provided to employee not directly related to trade or business unless taxable compensation to the employee	Follows House bill but • Also retains 50% deduction for food and beverage expenses associated with the operation of a taxpayer's trade or business • Expands 50% limitation to employer expenses associated with providing meals to employees through an eating facility considered a de minimis fringe benefit under current law • Disallows employer deduction for meals provided for the convenience of the employer through an employer-operated facility • Generally applicable to amounts paid or incurred after Dec. 31, 2017 • Elimination of meals deduction provided at the convenience of employer applies to amounts paid or incurred after Dec. 31, 2025; however, this provision would be repealed, effective for tax years beginning after Dec. 31, 2025, if certain revenue targets are met	Follows the Senate bill
Closed/frozen qualified plan nondiscrimination rules	Complicated coverage and nondiscrimination requirements must be satisfied	Special rules for closed/frozen plans making satisfaction of coverage and nondiscrimination testing easier	No provision	No provision
Deduction for excessive employee remuneration	$1M deduction limit for covered employee compensation with exceptions for commissions and performance-based compensation	Repeal of performance-based compensation and commission exceptions for $1M deduction limitation CFO added as a covered employee Status as covered employees continues after separation from service Expanded definition of applicable employer	Follows House bill Additional transition rule excepting binding contracts in effect Nov. 2, 2017 and unmodified on or after that date	Follows Senate bill with minor modifications to the transition rule
Qualified equity grants	No provision	Newly proposed Section 83(i) allowing election to defer gain on qualified equity (stock options and restricted stock units) for up to five years for certain private companies	Follows House bill. Also allows employees to make an inclusion deferral on statutory stock options. Generally would apply to stock exercised or options settled after Dec. 31, 2017	Follows the House bill, with changes related to who is eligible and what must be provided. Transition relief is to be provided for notice and participation requirements
Excise tax on excess tax-exempt organization executive compensation	See "Tax-exempt organizations" table	See "Tax-exempt organizations" table	See "Tax-exempt organizations" table	See "Tax-exempt organizations" table
Unrelated Business Taxable Income increased by certain fringe benefits	See "Tax-exempt organizations" table	See "Tax-exempt organizations" table	See "Tax-exempt organizations" table	See "Tax-exempt organizations" table

Compensation and benefits provisions				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
Dependent care assistance programs	Exclusion for amounts paid or incurred by an employer	Sunsets for tax years beginning after Dec. 31, 2022	No provision	No provision
Qualified bicycle commuting reimbursement	Excluded from income	No provision	Repealed for taxable years beginning after Dec. 31, 2017; provision sunsets Dec. 31, 2025	Follows Senate bill
Recharacterization of certain IRA and Roth IRA contributions	Taxpayers permitted to recharacterize contributions and conversion of IRAs	Repealed	Follows House bill	Follows House bill and Senate bill, but with a modification • Recharacterization of regular, annual contributions will be permitted, but not for Roth IRA conversions; thus, someone who converts a traditional IRA to a Roth IRA cannot change his or her mind after the conversion • Legislative history confirms that making an annual contribution to a traditional IRA and then converting it to a Roth (the "backdoor" Roth contribution) is permissible
In-service distributions from certain retirement plans	In service distributions permitted beginning at 62 for defined benefit plans and from section 457(b) state and local government plans beginning at 70½	Reduces age for in-service distributions to 59½ for eligible defined benefit and section 457(b) plans	No provision	No provision
Hardship distributions from retirement plans: Employee contributions	Prohibits employee contributions for six months after receiving a hardship distribution	No six-month prohibition on employee contributions after taking a hardship distribution	No provision	No provision
Hardship distributions from retirement plans: Amounts eligible for withdrawal	Withdrawals limited to employee contributions	Allows employees to take hardship distributions from a plan using account earnings, employer contributions, and employee contributions	No provision	No provision
Rollovers of plan loan offsets	60 days to contribute rollover of plan loan offset amount to an IRA to avoid taxable distribution	Extends permissible period for a rollover of loan offset to the due date (including extensions) for filing the return for the taxable year, if the offset is the result of termination of the plan or separation from service	Follows House bill, except that the offset must be as a result of termination of the plan, or the participant's termination of employment	Follows the Senate bill
Employer-provided housing	Excluded from income	Limits the exclusion to $50K ($25K for married individuals filing separately) Limited to one residence, and would phase out for highly compensated individuals and denied for 5% owners	No provision	No provision
Employee achievement awards	Excluded from income	Repealed	Allows exclusion but narrows definition of employee achievement award	Follows the Senate bill
Qualified moving expense reimbursements	Excluded from income	Repealed, although an exception applies for active-duty military members moving pursuant to a military order	Follows House bill, but effective for tax years beginning after Dec. 31, 2017, and sunsets on Dec. 31, 2025	Follows the Senate bill
Adoption assistance programs	Excluded from employee's taxable income	Repealed	No provision	No provision
Length of service awards for public safety volunteers	May defer up to $3K for length of service award	Not addressed	Increase from $3K to $6K	Follows the Senate bill
Archer Medical Savings Accounts (Archer MSAs)	Deduction permitted for employee contributions; employer contributions are excludible from income	Repealed. Maintains rollover of balances tax-free to health savings account	No provision	No provision
Provisions related to education	Exclusion of up to $5,250 of qualified education assistance	Repealed	No provision	No provision

Tax-exempt organizations

Provision	2017 law	House bill	Senate bill	Enacted legislation
Excise tax on private foundation investment income	Private foundations are subject to a 2% excise tax on their net investment incomes, but may reduce this excise tax rate to 1% by making distributions equal to the averages of their distributions from the previous five years plus 1%	Simplifies excise tax based on private foundation investment income by replacing present-law two-rate structure (2% and 1%) with a single rate of 1.4%	No provision	No provision
Investment income of private colleges and universities	Private foundations and certain charitable trusts are subject to excise tax of up to 2% on their net investment income; excise tax on net investment income does not apply to public charities, including colleges and universities	1.4% excise tax on net investment income of certain private colleges and universities with at least 500 students and with endowment assets of at least $250K per student; for these purposes, assets and investment income of related entities are treated as assets and investment income of the educational institution	Follows House bill with modifications: • Institution must have at least 500 tuition-paying students • Endowment-per-student threshold is increased from $250K to $500K • Clarifies that related-party rule generally applies only to assets and investment income intended or available for the use or benefit of the educational institution, and that an amount held by a related party cannot be taken into account with respect to more than one educational institution	Follows the Senate with modifications: • Applies to institutions with at least 500 students of whom more than 50% are located in the United States
Excise tax on excess tax-exempt organization executive compensation	No provision	20% excise tax for covered employees (generally, top five highest-compensated employees each year) receiving compensation in excess of $1M or excess parachute payments Covered-employee status continues regardless of whether individual remains a top five most highly compensated employee and after separation from service 20% excise tax also applies to severance payments to covered employees	Follows House bill	Follows the House bill with modifications: • Excise tax rate is 21% • Compensation subject to excise tax does not include amounts earned by licensed professional or paid to a licensed professional for the performance of medical or veterinarian services • IRS instructed to write regulations to prevent avoidance of tax through services as a nonemployee or through the use of pass-through or other entity to avoid such tax
Unrelated Business Taxable Income increased by certain fringe benefits	Tax-exempt entities may deduct certain fringe benefit expenses incurred in determining unrelated taxable income	Increases unrelated business taxable income by the amount of certain fringe benefit expenses for which a deduction would be disallowed if the employer were a for-profit organization	No provision	Follows House bill

Tax-exempt organizations				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
Unrelated Business Income Tax (UBIT) treatment of section 501(a) organizations	Current law is unclear regarding whether certain state and local entities (such as public pension plans) that are exempt under section 115(l) as government-sponsored entities that have also obtained tax-exempt status pursuant to section 501(a) are subject to the UBIT rules	Clarifies that an organization (such as a state pension fund) that is tax exempt or whose income is excluded from tax under a section other than section 501 (such as organizations that perform an essential governmental function that exclude income under section 115) and who have also obtained tax exemption under section 501(a) (so-called dual status organizations) are subject to the UBIT rules under section 511	No provision	No provision
UBIT treatment of research income	Income derived from a research trade or business is exempt from UBIT in the case of (1) research performed for the US or a state or political subdivision; (2) research performed by a college, university, or hospital for any person; and (3) research performed by an organization operated primarily to conduct fundamental research the results of which are freely available to the general public	Exclusion of research income from unrelated business taxable income for certain organizations limited to income from publicly available research	No provision	No provision
Qualification of art museums as private operating foundations	Private operating foundations (a form of private foundation that may use tax-free donations to fund their own activities rather than make grants to other charities) are exempt from a 30% excise tax on certain undistributed earnings that other private foundations must pay	Art museums will not qualify for private operating foundation status unless the museum is open to the public during normal business hours for at least 1,000 hours a year	No provision	No provision
Private foundation excess business holdings tax	In general, a private foundation may not own more than a 20% interest in a for-profit business, and any private foundation that does hold more than such an excess holding is subject to a 10% excise tax based on the value of that excess holding A private foundation that does not divest itself of excess holdings by the close of the subsequent year is subject to a 200% excise tax based on the value of the excess holdings	Excludes from the definition of a business enterprise: • Business 100% owned by the private foundation • Profits all distributed to the foundation (within specific timeframe) • Foundation interest acquired by means other than purchase • Independently operated	No provision	No provision
Political activity by section 501(c)(3) organizations	Charitable organizations may not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office	Temporarily allows 501(c)(3) organizations to make statements relating to a political campaign in ordinary course of their tax-exempt activities as long as they do not incur more than incidental incremental expenses, effective for taxable years beginning after Dec. 31, 2018; sunsets for tax years beginning after Dec. 31, 2023	No provision	No provision

Tax-exempt organizations				
Provision	**2017 law**	**House bill**	**Senate bill**	**Enacted legislation**
Reporting requirements for donor advised fund sponsoring organizations	An organization sponsoring donor advised funds must report on its Form 990 (1) the total number of donor advised funds it owns, (2) the aggregate value of assets held in those funds at the end of the organization's taxable year, and (3) the aggregate contributions to and grants made from those funds during the year; when seeking recognition of its tax-exempt status, a sponsoring organization must disclose whether it intends to maintain donor advised funds	Adds new Form 990 disclosures for sponsors of donor advised funds • The average amount of grants made from donor advised funds during the taxable year • Whether the organization has a policy with respect to donor advised funds relating to the frequency and minimum level of distributions from donor advised funds (sponsoring organization must include with its return a copy of any such policy)	No provision	No provision
UBIT computation for trade or business activities	Unrelated business income is calculated on an activity basis, but profits and losses from multiple activities may be netted against each other in order to calculate net unrelated business taxable income	No provision	Requires unrelated business income to be calculated for each unrelated activity and losses from one activity may not offset income from another; losses from an activity will carry forward and offset future income from the activity	Follows Senate bill
Charitable deductions for contributions to obtain the right to purchase college athletic event seating	Charitable deduction generally disallowed to the extent a taxpayer receives a benefit in return for a contribution, but a special rule permits taxpayers to deduct as a charitable contribution 80% of the value of a contribution made to an educational institution to secure the right to purchase tickets for seating at an athletic event in a stadium at that institution	No charitable deduction for payments in exchange for which the payer obtains the right to purchase college athletic event seating	Follows House bill	Follows House bill
Private activity bonds	Issued by state and local governments to finance the activities of or loans to private parties, with indirect benefits accruing to the state or locality issuing the bond; interest excluded from gross income and therefore exempt from regular income tax but not excludable under AMT	Interest on private activity bonds would be included in income and thus subject to tax, effective for bonds issued after 2017	No provision	No provision
Tax credit bonds	Various categories issued by state and local governments and other entities to finance specific types of projects Each category has its own set of rules regarding volume cap, if any, and allocation; bond holders receive federal tax credits fully or partially in lieu of interest payments from the issuer, depending on level of federal subsidy	Repeal; holders and issuers would continue receiving tax credits and payments for tax credit bonds already issued, but no new bonds could be issued Effective for bonds issued after 2017	No provision	Follows House bill
Professional sports stadium bonds	Some state and local governments have issued bonds to construct professional sports stadiums and successfully taken the position that bond interest is exempt from federal tax because the bonds are public purpose bonds	Interest on bonds issued to finance the construction of, or capital expenditures for, a professional sports stadium would be subject to federal tax, effective for bonds issued after Nov. 2, 2017 (date of introduction)	No provision	No provision
Advance refunding bonds	Interest on advance refunding bonds generally not taxable for government bonds but is taxable for private activity bonds	Repeal	Follows House bill	Follows House bill

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