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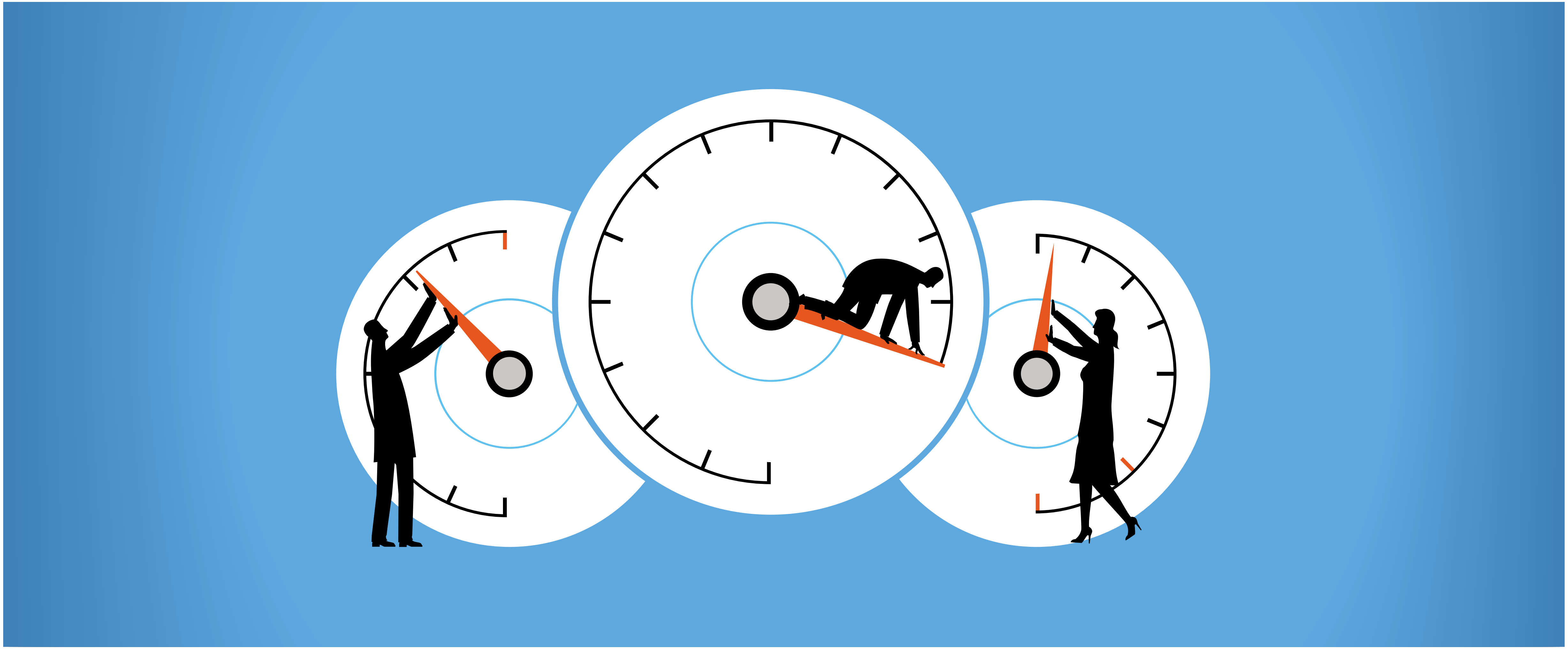

Tax Reform: What Dealers Need to Know

Disclosure

To ensure compliance with requirements imposed by the IRS, we inform you that any tax advice contained in this communication is not intended or written to be used, and cannot be used, for the purpose of avoiding penalties under the Internal Revenue Code.

This guidance concerning ASC 740 is preliminary and based on our current understanding of the indicated tax law provisions. Certain tax law provisions may be clarified through issuance of guidance by Treasury, regulations or future technical corrections. We will update our views as such further information becomes available.

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Agenda

- Tax Reform Changes for Individuals
- Corporate Provisions
- Pass-through Entities
- Tax Reform Changes for Businesses
- Estate and Gift Tax Changes

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Tax Reform Changes for Individuals

Tax Reform Changes For Individuals

- What Changed?
  - Tax Rates
  - Itemized Deductions
  - Standard Deduction
  - Affordable Care Act Items
  - And More….

Tax Reform Changes For Individuals

	New Law	Prior Law
Tax Rates	• 7 Brackets for each category • Top Rate for individual filers − 37% for amounts over $500,000 • Top rate for married filers − 37% for amounts over $600,000 • Effective for taxable years 2018 through 2025	• 7 brackets for each category • Top rate for individual filers − 39.6% for amounts over • Top rate for married filers − 39.6% − Effective for taxable years prior to 2017
Standard Deduction	• $24,000 - Married • $12,000 – Single − Effective for taxable years 2018 through 2025	• $12,700 - Married • $6,350 - Single − For 2017
Personal Exemption	• Repealed – taxable years 2018-2025	• $4,050 per individual (2017)

Tax Reform Changes For Individuals

	New Law	Prior Law
State and Local Taxes	• Itemized deduction not to exceed $10,000	• Itemized deduction for state and local taxes
Qualified Residence Interest	• Limit on acquisition indebtedness of $750,000 – Incurred after 12-31-2017 • Deduction for home equity indebtedness – Repealed • Effective for years 2018-2025	• Limit on acquisition indebtedness of $1,000,000 – Principal residence and – 1 other residence • Home equity indebtedness of $10,000
Child Tax Credit	• $2,000 per qualifying child • Limitation based on gross income exceeding $400,000 for a joint return ($200,000 for any other return) • Refundable portion cannot exceed $1,400	• $1,000 per qualifying child – Limitation based on gross income exceeding a threshold amount – Portion of the credit refundable

Tax Reform Changes For Individuals

	New Law	Prior Law
Charitable Contributions	• Cash contributions limited to 60% of the taxpayer's contribution base – 5 year carryover of excess over contribution base • Effective for tax years 2018-2025	• Contribution limited to 50% of taxpayer's contribution base – 5 year carryover of excess over contribution base
Casualty Losses	• Itemized deduction only for Federally declared disasters	• Itemized deduction
Miscellaneous deductions	• Repealed for tax years beginning after December 1, 2017 and before January 1, 2026	• Deductions allowed for amounts in excess of 2% of adjusted gross income

Tax Reform Changes For Individuals

	New Law	Prior Law
Overall limitation of itemized deductions	• Repealed for tax years beginning after December 31, 2017 and before January 1, 2026	• Limited based on adjusted gross income
Medical Expenses	• Deductible if in excess of 7.5% of adjusted gross income - Effective for years 2017 and 2018	• Generally deductible if in excess of 10% of adjusted gross income
Moving Expenses	• Deduction suspended for years 2018-2025	• Deductible if connected to work-related relocation
Alimony Expenses	• Repealed	• Deductible to payer
Alimony Income	• Not included in gross income of recipient – Divorce or separation agreements executed after 12-31-2018	• Includible in gross income of recipient

Tax Reform Changes For Individuals

	New Law	Prior Law
Alternative Minimum Tax	• Exemption amounts increased – $109,400 – joint return – $70,300 - individual return • Phase out of exemption amounts increased	• Exemption amount – $78,750 – joint return – $50,600 – individual return
Affordable Health Care Act (ACA)	• Eliminates the shared responsibility payment by reducing percentage to 0%. • Effective beginning after December 31, 2018	• Minimum essential coverage required of a monthly shared responsibility payment/penalty. • Lesser of 2 computational amounts multiplied by 2.5%

Polling Question

True or False- Under the new tax law, the child tax credit is $2,000 per qualifying child.

True

False

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Corporate Provisions

Corporate Tax Reform Provisions

- New 21% Rate
  - + Fiscal year taxpayers will pro rate
  - + Example: Fiscal Year End 6/30/18 Taxpayer
    - Total Taxable Income x 34% x 184/365
    - PLUS Total Taxable Income x 21% x 181/365
    - EQUALS Total Tax Due for FYE 6/30/18

- Corporate AMT Repealed
  - + AMT credit CF is refundable (50% partially refundable through 2020, remaining credits fully refunded in 2021)
  - + LIFO addback no longer an AMT issue

Deferred Taxes

- DTAs / DTLs must be re-measured for the effect of the change in tax law and rate
  - Reduced “federal benefit of state” effect on state effective tax rates
  - All re-measurement effects of deferred tax balances should be recorded to income from continuing operations as of the enactment date of 12/22/17
  - Impact of rate change will be a discrete item in the interim period in which law is enacted

Corporate NOLs

- NOL utilization limited to 80% of taxable income
- NOL carryback eliminated
- NOL carryforward period is indefinite

S Corp vs. C Corp – Several Considerations

- Rate differentials - 36% vs. 29.6% ETR for money taken out
- Is it beneficial if S Corp makes no distributions other than tax?
- Be cautious of new “unreasonable compensation” rules for C Corps if you are looking for other ways to take out cash
- No S Corp re-election for 5 years
- Stock basis differences between S Corp and C Corp can be important if there is a potential future sale
- State tax rates – differences for S Corps vs. C Corps
- Overall business entity structure

- **Bottom line…consult with your tax advisor!**

Polling Question

Which of the following are true statements about NOL?

a. NOL utilization is limited to 80% of taxable income
b. NOL carryback eliminated
c. NOL carryforward period is indefinite
d. All of the above are true

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Pass-through Entities

Pass-through Deduction

- Begins in 2018, sunsets at the end of 2025
- Effectively reduces the tax rate of pass-through income to 29.6% via a 20% deduction of pass-through income
- Does not apply for "specified service businesses"
- Applied at the partner/shareholder level

Pass-through Deduction - Formula

- Deduction is the lesser of:
  + 20% of "qualified business income" (QBI), but not in excess of the greater of:
    - (a) 50% of W-2 wages paid, OR
    - (b) Sum of 25% of W-2 wages paid + 2.5% of unadjusted basis of qualified tangible property
  + 20% of taxpayer's total taxable income less any net capital gain and qualified dividends

- 20% Deduction is not allowed in computing AGI but is a reduction to taxable income

"Qualified Business Income"

- Net domestic business income, gain, deduction, and loss with respect to qualified trade or business

- EXCLUDES:
  + Dividends, investment interest income, STCG/LTCG
  + Guaranteed payments paid to partners for services performed

Pass-through Deduction – Wage Limitation

- Wage limitation does not apply to taxpayers with taxable income <$315,000 (MFJ) or <$157,500 (Single)

- “W-2 Wages”: wages subject to withholding and paid by pass-through business during the calendar year ending during the taxable year of the taxpayer

- “Qualified tangible property”: held and available for use by taxpayer at the close of the taxable year, used in the production of QBI, either still being depreciated or purchased within the last 10 years

Pass-through Deduction – Wage Limitation Example

	Taxpayer #1	Taxpayer #2
Taxable Income	$450,000	$395,000
Cost Basis of Tangible Property	$150,000	$150,000
W-2 Wages	$0 – no employees	$0 – no employees
QBI	$25,000	$25,000
Wage Limitation Applies?	YES, taxable income over $415,000	Phased in over $100,000 $395,000 - $315,000 = $80,000 $80,000 / $100,000 = 80%
20% QBI	$5,000	$5,000
50% of Wages	$0	$0
25% of Wages + 2.5% Property	$3,750	$3,750
PASS-THROUGH DEDUCTION	**$3,750**	**$4,000** ($5,000 – ($5,000 – $3,750) * 80% phase in %)

Pass-through Deduction – Carryover Losses

- NOL provisions:
  - If pass-through net income is a loss, $500K is eligible to offset other individual income, the remaining loss carries forward to the next taxable year
  - This net loss reduces the following year's pass-through deduction
  - Consider this simple example:

	Income/(Loss)		**P-T Deduction**
QBI – Year 1 C/O	($2,000,000)	20%	($400,000)
QBI – Year 2	$2,500,000	20%	$500,000
Year 2 Pass-through Deduction Allowed			$100,000

Technical Termination Provision Change

- Technical Termination rule repealed where there is a sale or exchange of 50% or more of total partnership interests
  - Termination does take place if no part of the business carries on

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Tax Reform Changes for Businesses

Limitation on Business Interest Expense Deduction

- Generally limited to 30% of adjusted taxable income
- Floor plan interest expense remains 100% deductible
- Does not include investment interest

Limitation on Business Interest Expense Deduction

- Adjusted taxable income through 2021 resembles EBITDA
  + Taxable income
    - business interest expense, net
    - depreciation, amortization, and depletion
    - NOLs

Limitation on Business Interest Expense Deduction

- Adjusted taxable income after 2021 resembles EBIT
  - + Taxable income
    - business interest expense, net
    - NOLs

Limitation on Business Interest Expense Deduction

- Limitation determined at the filer level
- Carryforward tracked at the entity level, except for partnerships
- Double counting provisions complicate tiered structures
- Limitation carried forward indefinitely

Limitation on Business Interest Expense Deduction

- Does not apply to:
  + Small businesses with average annual gross receipts < $25M for the prior three years
  + Real estate businesses that make the election to use the alternative depreciation system (ADS) for certain property
    - Non-residential real property – 40 years
    - Qualified improvement property – 20 years

Recovery Period for Real Property

- Eliminates the separate definitions for qualified leasehold improvement, qualified retail, and qualified restaurant property
  + Now referred to as qualified improvement property
  + Generally defined as interior improvements to nonresidential real property after the initial placed-in-service date

- Forgot to provide 15-year recovery period

Bonus Depreciation (100% Expensing)

- Qualifying property acquired and placed in service from September 28, 2017 through December 31, 2022
- Phased down 20% a year over the 5 years (2023 – 2027)
- Property acquired before September 28, 2017, placed in service after September 27, 2017 follow old law (i.e. 50% for 2017, 40% for 2018, and 30% for 2019)

Bonus Depreciation (100% Expensing)

- Acquisition date for property acquired pursuant to a written binding contract is the date of such contract

- Used property is now eligible

- Property depreciated under ADS not eligible

Polling Question

True or False- Used property is not eligible for bonus depreciation.

True

False

Bonus Depreciation (100% Expensing)

- Bonus depreciation not available on any property used in a trade or business that has floor plan financing indebtedness
  - + Effective for tax years beginning after December 31, 2017
  - + It appears 100% bonus depreciation is available between September 28, 2017 and the end of the current tax year (December 31, 2017 for calendar year taxpayers)

Section 179 Expense

- Maximum yearly deduction increased to $1M

- Purchase threshold increased to $2.5M

- Effective for tax years beginning after December 31, 2017

Section 179 Expense

- Expands the definition of qualified property to include improvements made to nonresidential real property after the date the original property was placed in service:
  + Roofs, HVAC property, fire protection and alarm systems, and security systems

- Continues to be available to dealers

Polling Question

Under Section 179 expenses, the maximum yearly deduction increased to what amount?

a. $500k
b. $750k
c. $1 million
d. $1.5 million

Annual Depreciation Caps for Automobiles

- Base amount of depreciation increased to:

+ First year	$10,000
+ Second year	$16,000
+ Third year	$9,600
+ Fourth year & after	$5,760

Like-kind Exchanges

- Limited to exchanges involving real property not held for sale
- Applies to exchanges completed after December 31, 2017
- Transition rule included to exclude any exchanges in process at year-end
  + Property disposed of or replacement property received on or before December 31, 2017

Entertainment Expenses

- Deduction repealed for the following:
  - Entertainment, amusement, or recreation expense
  - Membership dues for any social club
  - Expenses related to a facility or a portion of a facility used in connection with any of the above
  - Fringe benefits including on-site athletic facilities and qualified parking and transportation benefits

Entertainment Expenses

- Retains but modifies the 50% deduction for food and beverage expenses, now included:
  + De minimis fringe benefits of food and meals
  + On-site eating facility
  + Meals provided on site for convenience of employer

Entertainment Expenses

- Starting in 2026, on-site meals and meals provided for the convenience of the employer become 100% nondeductible

- Holiday parties are still 100% deductible

- Contributions made to universities to purchase seating rights at an athletic event are now 100% nondeductible (used to be 80% deductible)

Polling Questions

What percentage of holiday parties are deductible?

a. 50%
b. 75%
c. 100%
d. Holiday parties are no longer deductible

Estate & Gift Tax Changes

Estate & Gift Tax Changes

- New Estate & Gift Tax Exclusion from 2018 to 2025 when it reverts to 2017 law in 2026

- Increased Exclusion to $10 million (indexed for inflation each year) which equals $11,180,000 for 2018 per person

- Retains the Prior Tax Law of Basis Adjustment ("step-up") at death

Estate & Gift Tax Changes

- Reduces the amount of Estates subject to the Estate Tax and creates opportunity for a window of time to significantly reduce Estate Taxes

- For Taxable Estates above $22,360,000 in 2018, the same planning techniques (sale of assets to a trust to freeze the value of the assets) are still appropriate

Estate & Gift Tax Changes

- New Tax Act represents a Paradigm Shift in planning for clients and advisors: concepts that were central to planning are no longer relevant
- Gifting currently uses of Carry Over Basis for assets; Assets Included in the Estate at Death receive the Step Up in Basis. This impacts the gain or loss when the asset is subsequently is sold

Estate & Gift Tax Changes

- With potential No Estate Tax for some clients, the New Tax Act makes "Income Tax is the new Estate Tax". Getting a Step Up in Basis at Death is more important under the New Tax Act

- This impacts what assets are currently gifted or sold (especially if the sale is not recognized for tax purposes) for taxpayers

Estate & Gift Tax Changes

- What Do You Need to Do? Review your current Estate Plan with your advisor taking into account the temporary changes from 2018 to 2025. Determine if any changes need to be made

- Consider additional Gift Transfers or Freeze Planning if your Estate is more than $22M before 2026 in case the Gift & Estate Exemption reverts back to 2017 level of $5.5M

Polling Question

True or False- The new tax law retains the prior tax law of basis adjustment ("step-up") at death?

True

False

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Thank You!

Questions?