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EFFECTS OF THE TAX CUTS AND JOBS ACT OF 2017

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by

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ABSTRACT

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Reformations of the tax law in the United States of America have always been tremendously complicated especially because they are used as a means to influence social policy. After the tax reform in 1986, the Tax Cuts and Jobs Act of 2017 was intended to bring about the most significant changes within the tax law of the country. Understanding the implementation of these changes is essential not only to all individuals but also to specific industries on a firm-wide level. Focus on key areas of changes made to the tax law through the execution of the TCJA highlight and simplify variations relevant to individual taxpayers and specific industries to allow for an increased efficiency in future planning. The multi-tiered bill passed by the House of Ways and Means committee was used as the subject of analysis in this study. For the chosen industries, an internal analysis of key parts of the act that directly affect the methodology they practice with their clients can prove to be tremendously useful in planning for the future.

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CHAPTER 1

INTRODUCTION

1.1 Introduction

While the tax law in the United States of America has gone through many significant changes over the years, none have been as extensive as the new Tax Cuts and Jobs Act of 2017 (TCJA). Formally 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 TCJA was signed by the 45th president of the United States Donald Trump on December 22, 2017. The administration stated four distinctive goals when modifying the old law and adopting the new one (White House Infographic). The first goal was to provide tax relief for middle – income families. The second goal was simplification for individuals, the third and fourth goal included economic growth and repatriation of overseas income. Congress aims on raising corporate output over the long – run and increasing the average household income by two major corporate tax reform . The first one being reducing the top marginal Federal tax rate from 35% to 21%. The second one being allowing firms to fully expense investments in nonstructural capital. The effects of the implantation of the new tax law on individuals, small businesses, the public health and real estate industries will become evident with time as will whether or not the TCJA achieved its original goals.

1.2 Purpose

The purpose of this research will be its contribution towards the clarification and simplification of information available to individual taxpayers. The research conclusions will conceivably also be used to relay relevant findings to the industries central to the case study. Standard perceptions regarding the new tax reform are hard to completely comprehend as they require in-depth research on the implementation and adoption of such changes. However, in the case of the aforementioned industries, certain sections of the new code have a more substantial impact on their customer base and their qualified business expenses. The intention of this study is to provide specific insight into the deductibility of qualified business expenses, and qualified business incomes, as well as the effects on international business. The second expected result of the study is to outline opportunities for further research as related to individuals and exempt entities in general based on any relevant findings. Implementing the new code in businesses is crucial to remain lawful within the context of the changes to the Internal Revenue Code that come with the TCJA.

CHAPTER 2

HISTORY OF THE TCJA

In June 2016 the House GOP released a document titled “A Better Way;” this document encouraged revisions to the then tax code. This reform was used as one of the social policies of Donald Trump’s political campaign. After Donald Trump was elected as the 45th president of the United States, on September 27th the administration released a 9-page document titled “Unified Framework for Fixing Our Broken Tax Code.” The document outlined the major intended goals of the reform and explored three main areas of the policy agreement between the House, Senate, and Administration, including tax relief and simplification for families, competitiveness and growth for job creators, and global competitiveness. According to the then Treasury Secretary Steven T. Mnuchin “This unified framework is the foundation Congress will use to craft legislation around middle-income tax cuts, a simpler and fairer tax code, and the most competitive business tax rates, so American companies of all sizes can create jobs, give their workers a pay raise, and grow the economy” (U.S. Department of Treasury).

On November 2, 2017, Kevin Brady the Chairman of the Ways and Means Committee released a legislative proposal H.R. 1, the Tax Cuts and Jobs Act. After various amendments, the proposal was approved by the Ways and Means Committee on November 9th. On November 16th the bill was approved by the House without any Democratic support. On November 28th the Senate Budget Committee voted to send the bill to the

Senate floor. On December 2, 2017, the Senate passed the bill with a simple majority. On December 22nd President Trump signed this legislation into law.

CHAPTER 3

INDIVIDUAL TAX REFORM

3.1 Ordinary Income Tax Bracket

Prior Law: Before the TCJA there were seven tax brackets applied to an individual's ordinary income ranging from 10% to 39.6% (U.S. Department of Treasury).

Unified Framework: Under the House Bill the administration's intention was to consolidate and simplify the division into four tax brackets: 12%, 25%, 36%, and 39.6% effective after 2017 (Unified Framework for Fixing our Broken Tax Code).

Current Law: the TCJA reform includes seven tax brackets with lower rates which took effect on January 1st, 2018 but ends after December 31, 2025 (H.R.1).

According to KPMG's Report on New Tax Law "The JCT has estimated that the new tax rate structure (subject to December 31, 2025 sunset) will decrease revenues by approximately $1.2 trillion over the 10 – year period. It is important for readers to note that lower tax bracket rates would generally mean lower tax payables, but since the calculation of taxable income is also changing all individuals might not necessarily experience a lower tax burden. The following tables sourced from Publication 5307 compare the old tax brackets to the new ones to provide a clearer picture of the differences in the new tax law.

Table 3.1: Single Taxpayer

OLD LAW		NEW LAW	
Tax Rate	Income Bracket	Tax Rate	Income Bracket
10%	$0 - $9525	10%	$0 - $9525
15%	$9526 - $38700	12%	$9526 - $38700
25%	$38701 - $93700	22%	$38701 - $82500
28%	$93701 - $195450	24%	$82501 - $157500
33%	$195451 - $424950	32%	$157501 - $200000
35%	$424951 - $426700	35%	$200001 - $500000
39.60%	$426701 and more	37%	$500001 and more

Table 3.2: Married Filing Jointly

OLD LAW		NEW LAW	
Tax Rate	Income Bracket	Tax Rate	Income Bracket
10%	$0 - $19050	10%	$0 - $19050
15%	$19051 - $77400	12%	$19051 - $77400
25%	$77401 - $156150	22%	$77401 - $165000
28%	$156151 - $237950	24%	$165001 - $315000
33%	$237951 - $424950	32%	$315001 - $400000
35%	$424951 - $480050	35%	$400001 - $600000
39.60%	$480051 and more	37%	$600001 and more

Table 3.3: Married Filing Separately

OLD LAW		NEW LAW	
Tax Rate	Income Bracket	Tax Rate	Income Bracket
10%	$0 - $9525	10%	$0 - $9525
15%	$9526 - $38700	12%	$9526 - $38700
25%	$38701 - $78075	22%	$38701 - $82500
28%	$78076 - $118975	24%	$82501 - $157500
33%	$118976 - $212475	32%	$157501 - $200000
35%	$212476 - $240025	35%	$200001 - $300000
39.60%	$240026 and more	37%	$300001 and more

Table 3.4: Head of Household

OLD LAW		NEW LAW	
Tax Rate	Income Bracket	Tax Rate	Income Bracket
10%	$0 - $13600	10%	$0 - $13600
15%	$13601 - $51850	12%	$13601 - $51800
25%	$51851 - $133850	22%	$51801 - $82500
28%	$133851 - $216700	24%	$82501 - $157500
33%	$216701 - $424950	32%	$157501 - $200000
35%	$424951 - $453350	35%	$200001 - $500000
39.60%	$453351 and more	37%	$500001 and more

3.2 Adjusted Net Capital Gain and Dividend Income Tax Bracket

TCJA did not change the taxation of adjusted net capital gains or qualified dividend income. The three brackets for capital gains and dividend income would remain constant at 0%, 15% and 20%. However, the bracket ceilings have been adjusted for inflation (Tacchino, 2).

3.3 Child Tax Credit

The changes made to child tax credits and qualifying dependent credits will be applied through the year 2025. Not only does the new law increase the child tax credit by almost double for every qualifying child, it also provides a nonrefundable credit for qualifying dependents other than children. The new law also increases the threshold before the phaseout begins. It does however require that a social security number be provided for each qualifying child for whom the credit had been claimed (Donaldson, 5). The following table sourced from Publication 5307 highlight these changes in comparison to the law before the enactment of TCJA.

Table 3.5: Changes to Child Tax Credit

Change	Old Law	New Law
Credit Allowed	$1000/child	$2000/child
Phaseout Floor for AGI MFJ	$110,000	$400,000
Phaseout Floor for AGI MFS & Head of Household	$75,000	$200,000
Phaseout Ceiling for AGI MFJ	$130,000	$440,000
Phaseout Ceiling for AGI MFS & Head of Household	$95,000	$240,000
Refund	15% of earned income in excess of $3000	15% of earned income in excess of $2500. Not to exceed $1400

The JCT estimates that these modifications will decrease revenues by $573 billion over the 10-year period, but the new SSN requirement will increase revenues by $30 billion in the same period (U.S. Department of Treasury).

3.4 Standard Deduction

The new law has significantly increased the standard deductions for all categories of tax payers. This modification is also set to expire at the December 2025 sunset. The idea behind considerably increasing the standard deduction amount is to discourage the use of itemized deductions in order to simplify the tax preparation process for individuals (H.R.1). The following table sourced from publication 5307 outlines the changes made to the allowable standard deduction amounts for individuals under separate categories.

Table 3.6: Standard Deduction

Filing Status	Old Law	New Law
Single	$6,500	$12,000
Married Filing Jointly	$13,000	$24,000
Married Filing Separately	$6,500	$12,000
Head of Household	$9,550	$18,000

According to JCT estimates, the modification the standard deduction amounts will decrease revenues by approximately $720 billion by the 2025 sunset (U.S. Department of Treasury).

3.5 Personal Exemptions

In terms of the old law a taxpayer could claim a personal exemption deduction of $4150. Married filing jointly individuals could claim two exemptions, additionally, taxpayers could claim exemption deduction for qualifying children and qualifying relatives. The amounts deductions would gradually be decreased if the taxpayer reached the AGI threshold for that category. However, the new law repeals the deduction for personal and dependency exemptions through 2025. The exemption amount for the years 2018-2025 is now zero (H.R.1). The JCT has estimated that this repeal of deductions and personal exemptions will increase revenues by approximately $1.21 trillion by the 2025 sunset date (U.S. Department of Treasury).

3.6 Education Expenses

The TCJA expanded the areas under "qualified higher education expenses" to include elementary, secondary, public, private, or religious schools. And it also includes materials and therapies for homeschooling. These expenses are now a part of the Section 529 plans and the earnings from these plans are not taxable for Federal purposes as long as they are used for qualified higher education expense purposes such as tuition, books, supplies, equipment, and room and board. However, the new law does cap the tax-free distribution amount to $10,000 per student when it comes to elementary and secondary school expenses. This limitation does not apply to post-secondary educational expenses (H.R.1). The JCT estimates that revenues will decrease by about $500 million because of this provision (U.S. Department of Treasury).

3.7 Other Changes Relevant to Individuals

A. In the case of individuals, itemized deductions for state and local income taxes, state and local property taxes, and sales taxes have been limited to an aggregate of $10,000. This cap is not applied to personal or real property taxes incurred in trade of business (H.R.1).

B. The new tax law eliminates the deduction of interest on qualifying home equity indebtedness. While under the old law qualified residence interest was allowed as an itemized deduction and included interest paid or accrued on debt incurred in acquiring, constructing or capitally increasing the value of a taxpayer's residence, none of these are now qualified to be itemized deductions (H.R.1).

C. The AGI limitation for charitable contributions of cash made to public charities and certain private charities was increased from 50% to 60% (H.R.1).

D. The TCJA limits the deduction of losses incurred that were not compensated by insurance or otherwise to only losses incurred in a federally declared disaster (H.R.1).

E. The new law suspends the use of miscellaneous itemized deductions. Under the law taxpayers could use this to deduct certain miscellaneous expenses as long as the aggregate of these expenses exceed the two percent AGI floor (H.R.1).

F. While under the old law the total amount of itemized deductions was reduced for individual taxpayers by 3% of the amount by which the taxpayers AGI exceeded a certain threshold, the new law has suspended this limitation. However, the taxpayer cannot lose more than 80% of the affected itemized deductions. This reform will be in effect till the 2025-year sunset (H.R.1).

G. Under the old law, a taxpayer could exclude up to $20 worth of reimbursement for qualified bicycle commuting expenses from their gross income, the new law suspends this exclusion. Under the new law the reimbursement of these expenses will be taxable. The JCT estimates that this will increase revenue by approximately $50 million (U.S. Department of Treasury).

H. With the implementation of the new law, the exclusion of reimbursement for qualified moving expenses has been suspended. The exclusion is however still in effect for U.S. Armed Forces members and their family members. The JCT estimates that this will increase revenues by approximately $4.8 billion (U.S. Department of Treasury).

I. The new law also aims to simplify the "kiddie tax" applicable to a child's unearned income calculation. Under the old law this income was taxed at the higher of the parents' tax rate or the child's tax rate. But under the new law the same rates are used for the child's unearned income that would be applied to ordinary and capital gains on trusts and estates.

J. Another reform that might be considered significant to the calculation of the individual taxable income implemented by the TCJA is the modification to the individual Alternative Minimum Tax (AMT). The following table sourced from publication 5307 highlights the changes made to individual AMT for all categories of individual taxpayers.

Table 3.7: Alternative Minimum Tax Exemption

	Old Law		New Law	
Category	Exemption	Phase-out threshold	Exemption	Phase-out threshold
MFJ	$86,200	$164,100	$109,400	$1,000,000
MFS	$43,100	$82,050	$54,700	$500,000
Individual/HoH	$55,400	$123,100	$70,300	$500,000

CHAPTER 4

HEALTHCARE

While the TCJA did not involve a lot of reforms to provisions for the Affordable Care Act (ACA), the one reform it did include is expected to have a significant impact on the act. The new law reduced the excise tax imposed on individuals who do not hold minimum required essential coverage to zero starting in 2019 (Glied, 1). Under the old law the individual shared responsibility provision in the ACA required individuals to be covered by a health plan that provided at least minimum coverage otherwise they would have been subject an excise tax.

While the JCT estimates that this will increase revenues by approximately $314 billion over 10 years, this reform does not have the 2025 sunset that most other reforms in the new law have (U.S. Department of Treasury). Although this provision is expected to generate revenues it is also predicted to have largely negative impacts on health insurance coverage. The CBO has estimated that this reform will reduce the number of people with health insurance by about $8-$9 million by the year 2027 since it directly reduces the number of people who choose to purchase insurance which will in turn raise premiums for individual insurance coverage.

Not only does the new law affect taxation for individuals as consumers of the healthcare industry, it also makes several significant changes that affect the taxation of the insurance industry as a whole. One such change made by the new law is that it changes the operations carryover and carryback periods for life insurance companies, these periods are now the same as they are for all other corporations.

Another interesting thing to be noted about the recent changes in tax law is that it makes numerous changes to the taxes imposed on beer, wine and distilled spirits. The new law reduces the amount of federal excise tax imposed on brewers and importers of beer. It also allows for brewers to transfer beer under bonds free of tax. In order to be able to do that the brewers would have to meet certain conditions (Glied, 2). These reforms, and other similar reforms on import of wine could arguably increase the production and sale of beer and wine in the country. From a health perspective, one could argue that increased production and availability of alcoholic beverages could have an indirect effect of increased rates of alcohol related health complications.

CHAPTER 5

SMALL BUSINESSES

Perhaps the most significant change brought about by the new tax law was the elimination of the progressive tax rate structures (Gale et al.). Instead of using income brackets for corporations to implement a tax rate like the previous law did, the new law imposes a flat rate of 21% on all corporations. The idea behind this reform is to make U.S. corporate tax rates more competitive relative to those imposed by other countries in order to boost the economy.

The new law also places an emphasis on reforms to make accounting methods for small businesses simpler. The JCT estimates that all the provisions affecting accounting methods for small businesses will result in a reduction of revenues by approximately $30.5 billion (U.S. Department of Treasury).

TCJA increases the threshold for the cash method of accounting. Before the implementation of the new law, C corporations or partnerships that had a C corporation partner, with some exceptions, could only use the cash method of accounting if the average gross receipts for the three prior tax years did not exceed $5 million (Gale, et al.). The provision for farm corporations and farm partnerships with a C corporation as a partner was that they could only use the cash method of accounting for prior years if their gross receipts did not exceed $1 million. After the implementation of the new law, the threshold for C corporations and qualified partnerships, and farm corporations has been increased to $25 million average.

Although, under the old law small businesses and corporations that had inventories could only use the accrual method of accounting for tax purposes with certain exceptions. The exception only applied to small businesses who had an average gross receipt of less than a $1 million. Another exception was provided for businesses in specific industries when their average gross receipts for the past three years did not exceed $10 million. Under the new law businesses with inventories can use the cash method as long as their average gross receipts for the past three ears does not exceed $25 million. This provision makes it easier for small businesses to switch to the cash method of accounting for the upcoming years (Gale, et al.).

The new law reforms the Uniform Capitalization rules for personal property acquired for resale. Producers or resellers with average gross receipts of $25 million over the last three years or less will be exempt from the UNICAP rules for real and personal property. Under the old law the threshold for this exemption was $10 million (Kess, 3).

The new law also increases the threshold for the exception for the accounting of long-term contracts. Under the old law to be exempt from using the percentage-of-completion method businesses had to have an average gross receipt of $10 million or less for the past three years (Kess, 2). Under the new law, this threshold has now been raised to $25 million so that corporations that qualify under this provision can use the completed-contract method to account for long-term contracts.

CHAPTER 6

REAL ESTATE

The TCJA bought into affect many changes regarding depreciation of assets for real estate owners. It is important to understand the reformations made by owners in order to decide whether to take Section 179 deductions or bonus depreciation (Weider, 1). There are also other changes that need to be considered before making this decision such as the excess loss limitation rules, and other state rules. This segment will discuss the changes to the Section 179 deduction, bonus depreciation and the excess loss limitation rules.

Prior to the enactment of the TCJA the allowable deduction for Section 179 was $510,000; this has been increased to $1 million post-TCJA. The maximum asset spending phaseout has also been increased from $2 million to $2.5 million (H.R.1). The new law now permits the deduction of qualified improvement of property and certain qualifies real property for non-residential properties.

Bonus deduction is allowable for both businesses operating at a loss and trusts. Under the new law the bonus depreciation has increased from 50% to 100% for qualified assets. This provision will sunset on January 1, 2023, after which the amount of bonus depreciation will decrease by 20% every year until 2026 (H.R.1).

The new law adds a limitation to the amount of net pass-through losses allowable to taxpayers every year. This limitation is applicable to all taxpayers other than certain corporations. The limitation is of $250,000 for single taxpayers and $500,000 for married taxpayers. Any business loss in excess of these threshold amounts will become a part of the taxpayer's net operating loss and is carried forward to the succeeding tax years. If the loss does not exceed the threshold but is still higher than the taxpayer's other income, it would still become a part of the taxpayer's net operating loss (Weider, 3). Therefore, these losses that are unavailable to be recorded as passive activity losses and still cannot be used to offset other income.

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BIOGRAPHICAL INFORMATION

Vaibhavi Nagar was born and raised in Indore, India. She moved to Texas in 2015 to pursue her undergraduate studies in accounting and finance. While attending the University of Texas at Arlington, she served as the President of Beta Alpha Psi – Gamma Phi chapter, Secretary of the Finance Society, and was a member of the Goolsby Leadership Academy, Cohort 14. While attending school, she also worked as a Lead Accounting Tutor for the IDEAS Center at the UTA Central Library. After graduation, she will pursue her master's degree. Her interests include tax accounting, finance, and data analytics.