H.R. 1 – The Tax Cuts and Jobs Act

Implications for Individuals and Businesses

Also

What to Expect in the Second Session of the 115th Congress

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Agenda

H.R. 1 – the Tax Cuts and Jobs Act

The Second Session Agenda:

Federal Spending – Omnibus Spending

Health Care

DACA

NAFTA

Tax Reform – Round 2?
Current Composition of the House:
- 238 Republican Members
- 193 Democratic Members
  - 4 vacancies – Franks (R-AZ), Conyers (D-MI); Murphy (R-PA); Tiberi (R-OH)
- 115th Congress Casualty list (as of 1/4/18):
  - Republicans -- 44 Members have departed or are departing (running for Senate, Governor, retiring, or resigned)
  - Democrats – 19 Members have departed or are departing (running for Governor, Senate, retiring, resigned, passed away)

Current Composition in the Senate:
- 51 Republican Members
- 47 Democratic Members
- 2 Independents (Caucus and vote with Democratic side)

In the Senate – need 60 votes to move legislation and certain nominations
- Filibuster – available for legislation – so need 60 for most legislation (except Reconciliation)
  > The recent change in the Senate rules eliminated the filibuster for Supreme Court nominees. In 2013, the rules were changed to eliminate the filibuster for all other judicial nominees as well as confirmable Administration positions (e.g., Cabinet Secretaries, and certain other positions below the Cabinet level)
- Reconciliation – only available for revenue changes, mandatory spending, and the debt ceiling
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2018 – Senate Races

Notes: †Angus King (I-ME) and Bernie Sanders (I-VT) caucus with the Democrats in the Senate.
*In Nov. 2018, both Minnesota and Mississippi will hold special elections for their Class II Senate seats concurrently with the regularly-scheduled elections for their Class I Senate seats. On the map, the shading on the left side of each state represents the rating for the regular election and the right side represents the rating for the special election.
H.R. 1625 – the Omnibus Spending Bill (Consolidated Appropriations Act, 2018)

- On Health care – what did not make it into the final bill:
  - Separate Republican and Democratic ACA stabilization packages – both offered/rejected
  - Changes to Medicare Part D coverage gap (donut hole) – pharmaceutical companies – remain liable for 70% of drug costs tied to the closure of the donut hole, rather than the 60%+ they wanted

- What made it into the Omnibus:
  - Roughly $4 billion to address the opioid crisis
    - $1 billion in new grants to states
    - $500 million – NIH research effort
    - $350 million – CDC – for prevention and surveillance (CDC receives $8.3 billion in total)
    - $300 million – law enforcement grant funding
    - $130 million – rural community support
  - Overall
    - $88 billion for HHS ($10 billion increase over 2017 levels)
    - $5.2 billion in total funding for FDA
  - Abstinence Education -- $25 million increase in funding

- Also – separate from the Omnibus – an attempt by Sen. Johnson (R-WI) to separately pass the “right to try” legislation via unanimous consent failed
H.R. 1 – A Focus on Business
(Unless otherwise stated, these provisions are permanent)

Corporations
- 21% corporate tax rate effective 1/1/18
- Disallows deduction for net interest expense to extend it exceeds 30% of EBITDA (through 2021) and EBIT thereafter
- Allows for 100% expensing for capital purchases – up to 2023; phases to zero in 20% increments each year thereafter
- Repeals corporate AMT
- Limits net operating losses to 80% of taxable income – carryforward indefinitely (carrybacks no longer allowed)
- Increases max. section 179 expensing amount to $1 million (reduced by the amount by which such cost exceeds $2.5 million)
- Moves to a territorial tax system for U.S. multinational companies (with base erosion/anti-abuse provisions)
- Impose a one time “deemed” repatriation tax on untaxed overseas earnings
  - 15.5% on earnings represented in cash/cash equivalents; 8% on all other earnings
- Limits non-recognition of gain from like-kind exchanges – to real property that is not held primarily for sale
- Repeals § 199 domestic production deduction – effective for taxable years beginning after 12/31/18
- Deduction for entertainment, amusement, recreation activities/facilities – generally disallowed – absent an exception

For Small Employers
- Allows taxpayers to use the cash method of accounting if annual average gross receipts for 3 prior taxable years do not exceed $25 million (certain pass through entities currently allowed to use cash method retain that right regardless of the new $25 million gross receipts test)
- Qualified Equity Grants for Non-Public Companies
  - Allows employees who are granted stock options or RSU’s as compensation for performance of services to elect to defer recognition of income for up to 5 years (if stock isn’t publicly traded) – subject to limitations
H.R. 1 – A Focus on Individuals
(Remember – most changes below expire after 2025)

7 New Brackets (represented below for joint filers):
- 10% (up to $19,500)
- 12% ($19k - $77k)
- 22% ($77k - $165k)
- 24% ($165k - $315k)
- 32% ($315k – 400k)
- 35% ($400k - $600k)
- 37% - over $600k
- Amounts indexed using chained-CPI-U (a permanent provision)

Child Tax Credit:
- Increased to $2,000 per child (of which $1,400 is refundable)
  - Phases-out for joint filers beginning at $400k
- Adds $500 credit for non-child qualifying dependents

AMT – retains, but...
- Increases exemption amount to $109,400 (joint filers) - $70,300 for all other taxpayers (except estates/trusts)
- Exemption amount phase-out increased to $1m for joint filers and $500k for all other taxpayers (except estates/trusts)

Estate Tax – retains, but...
- Essentially doubles the estate and gift tax exemption for estates of decedents dying and gifts made after 12/31/17 and before 1/1/26 – how? -
  - By doubling the exclusion amount from $5 million to $10 million (inflation adjusted going forward from 2012)
More Deductions

**Alimony**

- For any divorce/separation agreement executed after 12/31/18; or executed on/before that date but modified after 12/31/18 (if the modification specifically provides that H.R. 1’s changes will apply to such modification)
  - Alimony/separate maintenance payments no longer included in income of recipient or deductible by payor

**Qualified Moving Expense Deduction**

- Repealed for taxable years after 12/31/17 (exception for members of Armed Forces on active duty)

Retirement and Education Savings

**Retirement Savings**

- Effective 1.1.18 – a conversion from a traditional IRA, SEP or SIMPLE to a Roth IRA cannot be recharacterized
  - Recharacterizing amounts rolled over to a Roth IRA from 401(k) and 403(b) plans also prohibited
    - Roth IRA conversions made in 2017 may still be recharacterized as a contribution to a traditional IRA if the recharacterization is made by 10.15.18

**529 Plans – and ABLE Accounts**

- Allows 529 Plans to distribute up to $10k per year, per student, for enrollment at a public, private, or religious elementary and/or high school
- Allows 529 plan amounts to be rolled into an ABLE account without penalty
- Allows increased ABLE contributions in certain circumstances
Deductions

**Mortgage Interest**
- For new mortgages after 12.15.17 – the $1 million acquisition indebtedness limit reduced to $750k
  - Applies to homeowners with new mortgages on a first or second home – with $750k aggregate limit
  - For original mortgages incurred prior to 12/15/17, and refinanced after 12/15/17 – still eligible for $1 million limit
- Interest on home equity indebtedness incurred after 12/31/17
  - Treas. Guidance issued on 2.21.18 – may still be deductible if used to buy, build, substantially improve taxpayer’s home

**Standard Deduction**
- increased to $24k (joint) - $12k (single)
- Overall limit on itemized deductions – repealed
- Certain itemized deductions that are subject to the 2% of AGI floor - repealed

**Personal Exemption deduction** – repealed

**Charitable Deduction**
- Increases to 60% (up from 50%) the percentage of AGI limit on charitable contributions of cash to public charities
- Denies a charitable deduction for payments made in exchange for college athletic event seating rights

**Medical Expense Deduction**
- For 2018 and 2019 – the AGI threshold for deducting medical expenses is reduced to 7.5% (from 10%)

**Deduction for State and local income, property, and sales taxes** – repealed
- BUT – exception – allows a taxpayer to claim up to $10k deduction for aggregate of state/local property and income taxes (or sales taxes in lieu of income taxes). Exception does not apply to foreign real property taxes.
Pass Through Business Entities

- Through 2025, allows a 20% deduction for “qualified business income” earned through a pass through business (e.g., partnerships, S corporations, LLC’s, sole proprietorships) up to a certain income threshold:
  - The 20% deduction applies to the first $157,500 (single) and $315k (joint) of qualified business income earned by ALL businesses organized as a pass through entity
  - Above these thresholds (with a phase-in up to $207,500 (single) and $415,000 (joint)) - certain “specified service businesses” are precluded from the 20% deduction
    - E.g., fields of health, law, consulting, athletics, financial services, brokerage services, or any trade/business where principal asset is the skill/reputation of employees/owners (architects and engineers – found a way out of final bill)
  - For pass through entities (other than “specified service businesses) above these income thresholds, the deductible amount would be the lesser of:
    1. 20% of the taxpayer’s qualified business income or
    2. the greater of:
       a. 50% of the W-2 paid with respect to the qualified trade/business, or
       b. Sum of 25% of W-2 wages with respect to the qualified trade/business, plus 2.5% of unadjusted basis, immediately after acquisition, of all qualified property

Other

*The Affordable Care Act* (a permanent provisions – does not sunset)

- Repeals the ACA’s individual mandate (essentially – reduces to “zero” the “shared responsibility payment” for individuals that fail to maintain minimal essential coverage)
Short-term Issues in 2018

Funding the Federal Government (Appropriations)

- *Funding for Federal Operations (beyond January 19)* – the goal is an omnibus funding bill that funds government operations through the end of the fiscal year on 9.30.18. Because this is “must pass” legislation, could be vehicle for the following:
  - Extensions of expiring programs such as CHIP (Children’s Health Insurance Program); National Flood Insurance Program; Section 702 of the Foreign Intelligence Surveillance Act (FISA)
  - Extension of the expired moratorium on the medical device tax (expired 12/31/17)
  - The January 20th deadline for either lifting the Budget Control Act’s mandated caps for defense and domestic discretionary spending or face automatic budget sequestration
  - Supplemental disaster relief funding
    - In December 2017 – the House passed an $81 billion relief package – has yet to be considered in the Senate
    - Deferred Action for Childhood Arrivals (DACA)

Longer Term 2018 Issues

- Sometime – likely March/April timeframe – increasing the debt ceiling
- Extending certain expired/expiring tax provisions (not tax reform)
- Legislation to make technical corrections to H.R. 1 – the Tax Cut and Jobs Act
- Infrastructure spending – one potential area of bi-partisan movement
- Entitlement Reform (Welfare focus)
- NAFTA

One Caveat – the primary season kicks-off in earnest on March with the Texas and Illinois primaries, and heats up in May and June with primaries on the majority of states – this will affect the Congressional schedule in 2018
Disclosures

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