SUBJECT: **Tax Reform 2018 - New Tax Deduction for Qualified Business (pass-through) Income**

THE FLORES GROUP

BUSINESS & TAX ADVISORS

IN THIS ISSUE

Dear Clients & Friends:

The Flores Group provides international corporate and tax services to international investors and business persons. We have over 30 years of experience dealing with complex business and international structures and transactions. We have experienced bilingual Attorneys and CPA's to assist you with your legal, tax, and business projects. We are providing this Alert for your review and consideration.

Tax Reform 2018

The U.S. Congress and Senate approved the Tax Reform as presented by the U.S. Congress and Senate Conference Committee. The Tax Bill has significant changes that affect individuals, corporations and businesses. A significant new tax deduction taking effect in 2018 under the new tax law, should provide a substantial tax benefit to individuals with "qualified business income" from a partnership, S corporation, LLC, or sole proprietorship. This income is sometimes referred to as "pass-through" income.

20% Deduction for Qualified Business (pass-through) Income

The deduction is 20% of your "qualified business income (QBI)" from a partnership, S corporation, or sole proprietorship, defined as the net amount of items of income, gain, deduction, and loss with respect to your trade or business. The business must be conducted within the U.S. to qualify, and specified investment-related items are not included, e.g., capital gains or losses, dividends, and interest income (unless the interest is properly allocable to the business). The trade or business of being an employee does not qualify. Also, QBI does not include reasonable compensation received from an S corporation, or a guaranteed payment received from a partnership for services provided to a partnership's business.

The deduction is taken "below the line," i.e., it reduces your taxable income but not your adjusted gross income. But it is available regardless of whether you itemize deductions or take the standard deduction. In general, the deduction cannot exceed 20% of the excess of your taxable income over net capital gain. If QBI is less than zero it is treated as a loss from a qualified business in the following year.

Rules are in place (discussed below) to deter high-income taxpayers from attempting to convert wages or other compensation for personal services into income eligible for the deduction.

Taxpayers that Qualify

For taxpayers with taxable income above $157,500 ($315,000 for joint filers), an exclusion from QBI of income from "specified service" trades or businesses is phased in. These are trades or businesses involving the performance of services in the fields of health, law, consulting, athletics, financial or brokerage services, or where the principal asset is the reputation or skill of one or more employees or owners.

Here's how the phase-in works: If your taxable income is at least $50,000 above the threshold, i.e., $207,500 ($157,500 + $50,000), all of the net income from the specified service trade or business is excluded from QBI. (Joint filers would use an amount $100,000 above the $315,000 threshold, $415,000.) If your taxable income is between $157,500 and $207,500, you would exclude only that percentage of income derived from a fraction the numerator of which is the excess of taxable income over $157,500 and the denominator of which is $50,000. So, for example, if taxable income is $167,500 ($10,000 above $157,500), only 20% of the specified service income would be excluded from QBI ($10,000/$50,000). (For joint filers, the same operation would apply using the $315,000 threshold, and a $100,000 phase-out range.)

Phase Out of Deduction

Additionally, for taxpayers with taxable income more than the above thresholds, a limitation on the amount of the deduction is phased in based either on wages paid or wages paid plus a capital element. Here's how it works: If your taxable income is at least $50,000 above the threshold, i.e., $207,500 ($157,500 + $50,000), your deduction for QBI cannot exceed the greater of (1) 50% of your allocable share of the W-2 wages paid with respect to the qualified trade or business, or (2) the sum of 25% of such wages plus 2.5% of the unadjusted basis immediately after acquisition of tangible depreciable property used in the business (including real estate).

So if your QBI were $100,000, leading to a deduction of $20,000 (20% of $100,000), but the greater of (1) or (2) above were only $16,000, your deduction would be limited to $16,000, i.e., it would be reduced by $4,000. And if your taxable income were between $157,500 and $207,500, you would only incur a percentage of the $4,000 reduction, with the percentage worked out via the fraction discussed in the preceding paragraph. (For joint filers, the same operations would apply using the $315,000 threshold, and a $100,000 phase-out range.)

Other limitations may apply in certain circumstances, e.g., for taxpayers with qualified cooperative dividends, qualified real estate investment trust (REIT) dividends, or income from publicly traded partnerships.

Conclusion

The Flores Group would be very pleased to help analyze your tax implications. We hope this information is helpful in analyzing your legal and tax obligations in Texas and the USA. The material is meet as a general discussion and not intended to be specific legal or tax advice. You should consult with your legal or tax advisors for your specific situation.

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SOURCE: THOMSON REUTERS / TAX & ACCOUNTING

This information is a presentation of the general rules and should not be used or relied upon for any particular investment or transaction. We recommend you consult your tax attorney or advisor for your specific situation. If you would like more information on these matters we would be glad to visit with you.

Click here to visit our website for more information: Flores Group

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