



## Legal Alert: Tax Reform Executive Summary – A 2-Pager on the 7 Things You Need to Know

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Tax reform efforts, if successful, will have a major impact on virtually every business. There has been a great deal of reporting on the tax reform process and the proposed changes to the US Internal Revenue Code (IRC). This Alert provides a high-level overview of the top 7 tax reform issues that all executives need to know:

- Current status of tax reform
- Tax rate for corporations and partnerships and other pass-through income
- Limitations on interest deductibility
- Immediate deductibility of otherwise capital costs
- Changes to the US international tax system
- State and local tax impacts
- Compensation and benefits provisions

Tax reform is rapidly evolving. For up-to-date information on the current state of tax reform, visit the Eversheds Sutherland [Tax Reform Law blog](#). For more detailed analyses, see the prior Eversheds Sutherland alerts on the [House tax reform bill](#) and the [Senate tax reform bill](#).

### 1. Current Status of Tax Reform

- House: The tax writing committee of the House -- the Committee on Ways & Means -- passed a tax reform bill on November 9, which was then passed by the full House on November 16 (the House Plan).
- Senate: The tax writing committee of the Senate -- the Senate Finance Committee -- passed a tax reform bill on November 16 (the Senate Plan) that had many similarities with, but also a large number of differences from, the House Plan. The Senate Plan is under consideration by the Senate but may be substantially modified before being voted on by the full Senate.
- President: A bill will arrive at the White House for the President's consideration only if the House and the Senate agree on a unified tax reform bill that passes both chambers.

### 2. Changes to the Tax Rate

- Corporate tax rate: The statutory corporate tax rate would be lowered from 35 percent to 20 percent. The House Plan makes this change effective for 2018, whereas the Senate Plan makes this change effective for 2019.
- Partnerships and other pass-throughs: The House Plan generally creates a maximum 25 percent rate for qualified business income. The Senate Plan generally permits individuals to deduct 17.4 percent of domestic qualified business income from pass-through entities (thus reducing taxable income).

### 3. Limitations on Deductibility of Interest

- General rule: Limits the ability to deduct interest to 30 percent of adjusted taxable income.
- Multinational groups: US corporate members of multinational groups are subject to a second limitation on interest deductibility if the US members are disproportionately leveraged as compared to the worldwide group.
  - Under the House Plan, this provision applies if the US group's share of the global group's net interest expense exceeds 110 percent of the US group's share of the global group's EBITDA.
  - Under the Senate Plan, the provision applies if the debt-to-net-tax-basis ratio of the US members exceeds 110 percent of the debt-to-net-tax-basis ratio of the worldwide group.
  - The limitation on multinational groups applies in addition to the general rule discussed above, with a taxpayer being subject to the more restrictive of the two limitations.

### 4. Immediate Deductibility

- General rule: Companies would be entitled to 100 percent bonus depreciation for property placed in service after September 27, 2017, and before January 1, 2023.
- Expansion of qualifying equipment: Under the House Plan, bonus depreciation also would be allowed not only for new equipment, but also for used equipment. The Senate Plan does not include any such expansion (but does shorten the depreciation periods for certain longer life property).

## 5. Changes to the US International Tax System

- Transition rule: Subjects previously untaxed earnings of certain foreign subsidiaries to a one-time transition tax, at a reduced rate, payable over 8 years.
- Dividends received deduction: Generally provides a 100 percent deduction for dividends received from certain foreign subsidiaries.
- Minimum tax: Generally imposes a minimum tax on the combined income of controlled foreign subsidiaries.
- Related party payments: Significantly limits the ability to claim US tax deductions for payments to related foreign persons.

## 6. State and Local Tax

- Deductibility: Although the proposals call for reducing or eliminating state and local tax deductions for individuals, businesses would still be entitled to deduct state and local taxes.
- Adjustments to federal taxable income: Many states calculate tax by referencing federal taxable income. In these states, increases and decreases to federal taxable income will increase or decrease state taxable income. For example, greater depreciation deductions and limited interest expense deductions (referenced above) will have a similar effect on taxable income in several states.

## 7. Compensation and Benefits

- Deductible compensation: Expands the \$1 million cap on deductible compensation paid by public companies by eliminating the exception for performance-based compensation, covering companies with public debt even if the company is not publicly traded, and widening the scope of covered officers subject to the cap.
- Deferred compensation: Both the House Plan and the Senate Plan initially proposed to do away with most deferred compensation, making compensation taxable when it is no longer subject to a substantial risk of forfeiture. This provision was removed from both the House and Senate Plans.

### ***Eversheds Sutherland Observations:***

- The Senate currently is working to modify the Senate Plan in an effort to line up the 50 votes required for passage as well as to provide some compromises to help align the Senate Plan with the House Plan. We expect that if a tax reform bill reaches the White House, the President would sign the bill into law.
- The reduction in rates is coupled with a number of limitations on deductions and other changes to the IRC, including those described above. Consequently, the actual impact of a statutory rate reduction on the effective tax rate of a particular company may vary significantly.
- The prospects for passage of a tax reform bill remain unclear. However, the tax departments of most businesses have undertaken significant efforts to understand the potential impact of these tax reform proposals. In that regard:
  - Businesses should consider tax planning opportunities, including strategies to potentially defer income and accelerate deductions, in light of the proposed tax rate reductions.
  - Financial statement implications of tax reform also must be considered, such as the impact of tax rate reductions on the amount of deferred taxes reported on a company's balance sheet.

*If you have any questions about this legal alert, please contact the Eversheds Sutherland attorney with whom you regularly work, or to be connected with a member of the Eversheds Sutherland tax team, please contact Taylor Kiessig, Esq. at 202.383.0844 or [taylorkiessig@eversheds-sutherland.com](mailto:taylorkiessig@eversheds-sutherland.com)*