10 Big Takeaways for Michigan CPAs on the New Tax Law

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The 'Tax Cuts and Jobs Act' is now signed and final. The act is very comprehensive and makes significant changes to many provisions of the Tax Code. The following are 10 substantial provisions affecting Michigan CPAs and their clients.

1. **The Big One: QBI and New Section 199A.** One of the most far-reaching changes to the Code is the new pass-through taxation and the decoction for 'Qualified Business Income', or QBI.

2. **QBI is on Taxable Income**. QBI is a deduction to taxable income and not AGI. Accordingly it appears that QBI will not apply to Michigan income tax calculations.

3. **Income Threshold to QBI.** The QBI deduction applies to the first $315,000 of joint income (subject to phase-out of $100,000 of additional income; $157,500 of income if single, phased-out with an additional $50,000 of income) earned from businesses organized as S-corporations, partnerships, LLCs, and sole proprietorships. Limitations based on W-2 wages and capital apply above those amounts and for "specified service businesses." The income threshold exemption applies to service businesses, so CPA firms, law firms, and other service entities with income below the threshold can deduct QBI. We call this the 'Poor CPA' exception. A major issue will be reasonable comp.

4. **Cash Method of Accounting.** The Cash method of accounting is expanded from the old threshold of $5 million of average gross receipts from all prior years to a more generous annual average $25 million of gross receipts for the three prior years. The $25 million is indexed for inflation for years beginning after 2018. This will

5. **Completed Contract**. The completed contact method for long-term construction contracts can now be used if the contract is expected to be completed (at the time it is entered into) within two years, and the taxpayer has an annual average gross receipts of not more than $25 million.

6. **Interest Deduction for Businesses.** The new law restricts net interest expense deductions to 30% of adjusted taxable income. The law exempts taxpayers with average annual gross receipts of $25 million or less for the three-tax-year period ending with the prior tax year. The limitation does not apply, at the taxpayer's election, to any farming business or to a real property trade or business as defined in §469(c)(7)(C). The limitation also does not apply to certain regulated public utilities. The limitation on interest deduction will affect Michigan tax on larger entities, and remain deductible for smaller entities.

7. **NOL.** The old law of NOL carry-back for 2 years and a NOL 20-year carry-forward is repealed and replaced with an indefinite carry-forward of up to 80% of taxpayer's taxable income. NOLs for farming losses have a special two-year carry-back. Sub-S and LLC NOLs are applied on the owner level, and are applied after the application of

the passive loss rules of §469. The NOL rules will affect pass-throughs and consequently affect Michigan taxes, by eliminating the carry-back.

8. **Bonus Depreciation.** Under the new Law, bonus deprecation for qualified property placed in service after September 27, 2017 and before January 1, 2023 (or January 1, 2024 for certain qualified property, including certain aircraft) is 100%, or full expensing. The bonus depreciation is then phased down to 80% for 2024 and reduced by 20% for every year thereafter. The definition of qualified property is under §168(k)(2). Bonus depreciation will change Michigan income tax by virtue of the pas-through provisions.

9. **AMT:** Partly gone. Corporate AMT is repealed, but individual AMT remains with a higher threshold. AMTI is now $70,300 for singles and $109,400 for married couples.

10. **Specific industries and entities affected.** There are special rules for agriculture (NOL and interest), construction (completed contract). Some additional rules change for nonprofits. In general, business entertainment is restricted.