TAX UPDATE

3/28/2018

2018 Budget Act Brings Additional Tax Changes

On February 9, President Trump signed the Bipartisan Budget Act of 2018 (BBA), ending a brief government shutdown. This 2-year budget contains a host of tax law changes. We have highlighted the primary areas the bill covers below.

Tax Extenders Retroactive through 2017

The BBA extends for one year a set of tax provisions, known as “extenders,” which expired at the end of 2016, including:

- **Exclusion of discharge of mortgage debt.** The BBA extends homeowners’ ability to exclude from gross income mortgage debt on a principal residence that was forgiven in 2017 (for example, as a result of a foreclosure, short sale or loan modification). It also modifies the exclusion to make it apply to debt discharged later than 2017 but according to a written agreement that was entered into in 2017. Without the extended provision, taxpayers would have to pay income taxes on the amount of mortgage debt forgiven.

- **Deductibility of mortgage insurance premiums.** Taxpayers can continue to treat mortgage insurance premiums paid or accrued in 2017 as deductible interest. But this affects only taxpayers who itemize their deductions, and changes under the Tax Cuts and Jobs Act (TCJA) are expected to significantly reduce the number of taxpayers who do so. Further, the deduction phases out for taxpayers with adjusted gross income (AGI) of $100,000 to $110,000.

- **Deductibility of qualified tuition and related expenses.** “Above-the-line” deductions are subtracted from a taxpayer’s gross income to calculate AGI. The BBA extends through 2017 the above-the-line deduction for higher education expenses. Taxpayers needn’t itemize to take advantage of the deduction, but it’s capped at $4,000 for individuals with AGI that doesn’t exceed $65,000 ($130,000 for joint filers) and $2,000 for individuals with AGI that doesn’t exceed $80,000 ($160,000 for joint filers).

- **Incentives for empowerment zones.** Empowerment zones are located in economically distressed areas. The BBA extends through 2017 the tax incentives — including tax-exempt bonds, employment credits, increased expensing and certain gain exclusion — for certain businesses and employers to operate in empowerment zones.

- **Multiple renewable energy, energy-efficient property and vehicle provisions.** Construction of qualified renewable energy facilities in 2017 are eligible for tax credits. Buyers and builders of energy efficient residential and commercial properties are eligible to take advantage of tax credits and deductions for properties acquired or put into service in 2017, with certain residential property and solar credits available through 2021. Similarly, credits and bonus depreciation allowances for producers and purchasers of fuel cell vehicles, alternative fuel vehicles, certain electric vehicles as well as producers of alternative fuels are extended through 2017.

Additional Tax-Related Provisions

The BBA also contains several other provisions that could affect federal taxes, including those related to:

- **Estimated corporate tax payments.** The BBA repeals a rule in the Trade Preferences Extension Act of 2015 regarding the payment of certain estimated corporate taxes. The rule would have required corporations with assets of at least $1 billion to increase the amount of the estimated taxes installment due in July, August or September of 2020 by 8%, with the next required installment (due in October, November or December of 2020) reduced accordingly.

- **Excise tax on private investment income for colleges and universities.** The 1.4% excise tax imposed on net investment income for institutions with at least 500 students, assets of at least $500,000 per student, and with at least half of the student population located in the U.S. The BBA has clarified that these students are defined as tuition-paying students, effective January 1, 2018.

- **Private foundation excessive business holdings tax exemption.** Starting in 2018, private foundations might be excepted from excess business holdings taxes, provided they meet the following criteria:
    (1) The foundation owns all of the business enterprise's voting stock at all times during the tax year,

(2) The foundation acquired all of its interests in the for-profit business other than by purchasing it,
(3) The business enterprise distributes all of its net operating income for any given tax year to the private foundation within 120 days of the close of that tax year,
(4) The directors, executives, etc. of the business enterprise are not substantial contributors to the private foundation,
(5) At least a majority of the board of directors of the private foundation are persons who are not directors or officers of the business enterprise or family members of a substantial contributor to the private foundation, and
(6) There is no loan outstanding from the business enterprise to a substantial contributor to the private foundation or to any family member of such a contributor.

- **Natural disasters in California and elsewhere.** The BBA provides tax relief for people affected by the 2017 California wildfires. That includes an employee retention tax credit and special rules regarding early distributions from retirement plans and deductions for personal casualty losses due to the fires. It also temporarily suspends charitable contributions limitations to qualified California disaster relief organizations for contributions made between October 8, 2017 and December 31, 2018. The BBA also extends similar tax relief that had previously been provided to eligible taxpayers in disaster areas hit by Hurricanes Harvey, Irma and Maria.

- **Flexibility around 401(k) contributions after a hardship distribution.** Employees who use their 401(k) plans in times of financial hardship are no longer prohibited from making contributions back to their plan or other modifications within 6 months of a hardship distribution. This is effective for plan years starting in 2019.

- **Whistleblower awards.** Two amendments clarifying whistleblower rights made their way into the BBA. The first makes clear that whistleblowers awarded money under the Dodd-Frank Act and state False Claims Acts — not just under the Federal False Claims Act and federal tax laws — are entitled to an above-the-line tax deduction for their attorneys' fees. This treatment starting in 2018 prevents double taxation of the fees (first as part of the entire amount received by the whistleblower and again on the amount paid to the attorney).

What Do I Need to Do?

As always in times of change, we strongly encourage all our clients to be in close communication with us and their other advisors. The IRS has indicated that it's reviewing the BBA and plans to provide additional information as quickly as possible.