2018 Federal Tax Update

MARCH 10, 2018

CNMI DISTRICT COURT CONFERENCE

H.R. 1
https://www.congress.gov/bill/115th-congress/house-bill/1/text

Passed by U.S. Congress in December 2017

Amends Internal Revenue Code of 1986

The tax rate has changed, from 2018 through 2025.

Old Law	New Law	Difference
10%	10%	--
15%	12%	3%
25%	22%	3%
28%	24%	4%
33%	32%	1%
35%	35%	--
39.6%	37%	2.6%

The income limits for the brackets has increased.

Before, you were in the 25% bracket up to $153,100 MFJ

Now, you are in the 22% bracket up to $176,550

The top tax rate of 37% for 2018 to 2026 only applies if your taxable income is more than $600k for MFJ, $500k for HOH or single

This is a significant increase from 2017 limits $470,400 MFJ $418,400 for single

Penalty on tax preparers

If a preparer fails to comply with due diligence requirements with respect to determining eligibility to file as head of household or AOTC, ACTC shall pay a penalty of $500 for each such failure

DEDUCTION FOR QUALIFIED BUSINESS INCOME OF PASS-THRU ENTITIES

The intent is to provide some relief to S corps and LLCs because of the reduction in the C corp tax rate

For taxpayers other than corporations (i.e. sole proprietorship, LLC, S corporation or partnership) there is a deduction equal to the sum of

(1) the lesser of –

  (A) the combined qualified business income, or

  (B) 20% of the excess (if any) of -

    (i) taxable income of the taxpayer, over

    (ii) the sum of any net capital gain, plus the aggregate amount of the qualified cooperative dividends, of the taxpayer, plus

(2) the lesser of –

  (A) 20% of qualified cooperative dividends, or

  (B) taxable income (reduced by net capital gain of the taxpayer

What is combined qualified business income?

(1) IN GENERAL – the term combined qualified business income amounts means an amount equal to -

(A) the sum of the amounts determined under paragraph (2) for each qualified trade or business, plus

(B) 20% of qualified REIT dividends and qualified PTP income of the taxpayer

(2) Determination of Deductible Amount for Each Trade or Business

The lesser of
(A) 20% of the taxpayer's qualified business income, or
(B) the greater of –
  (i) 50% of W-2 wages, or
  (ii) 25% of W-2 wages, plus 2.5% of the unadjusted basis immediately after acquisition of all qualified property

Example:
Revenues $500,000
Salaries and wages $300,000
Other expenses $100,000
Capital gains $20,000
Profit $120,000 (\$500k-\$300k-\$100k+\$20k)
Qualified property $80,000

Start with the lesser of 20% of qualified business income – in this case $24,000 or the greater of 50% of W-2 wages – in this case $150,000 or

Then calculate 25% of W-2 wages – in this case $75,000.
Then calculate 2.5% of qualified property – in this case $2,000.
Add these two to get $77,000.

So the greater of 50% of wages or 25% of wages plus 2.5% of property is $150,000.

Since 20% of income is less than $150,000 we would use the $24,000 figure.

The deduction can be phased out.

Threshold amount is $157,500 single and $315,000 MFJ

No limit if your taxable income is lower than these figures.

If it is higher, but is less than $207,500 ($415,000) and the amount determined under 2(B) with respect to any qualified trade or business carried on is less than the amount determined in 2(A) then paragraph 2 shall be applied without regard to 2(B) and by reducing the amount determined in 2(A) by the following:

The reduction is the amount which bears the same ratio to the excess amount as

(1) the amount by which taxable income exceeds the threshold amount bears to
(2) $50,000 (or $100k for MJF)

The excess amount is the excess of the amount determined under 2(A) over the amount determined in 2(B)

QUALIFIED BUSINESS INCOME

The net amount of qualified items of income, gain, deduction and loss with respect to any qualified trade or business of the taxpayer.

If the net amount is a loss, it is treated as a loss from a qualified trade or business in the succeeding taxable year

Qualified items of income, gain, deduction and loss means items that are effectively connected with the conduct of a trade or business in the U.S. (CNMI) and is included in determining taxable income.

It does not include capital gains or losses or dividends or interest income other than interest income which is properly allocable to a trade or business

and a few other items (CFC, notional principal)

Qualified business income does not include

(A) reasonable compensation paid to the taxpayer for services rendered to the business

(B) guaranteed payments to a partner for services rendered to the business

(C) to the extent provided in regs, any payment in section 707(a) to a partner for services rendered to the business

QUALIFIED TRADE OR BUSINESS

QTB means any trade or business other than

(A) a specified service trade or business, or
(B) performing services as an employee

Specified trade or business means any trade or business other than engineering and architecture, or which involves services that consist of investing and investment management, trading, or dealing in securities, partnership interests, or commodities

(3)(A) any trade or business involving the performance of services in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services, or any trade or business where the principal asset of such trade or business is the reputation or skill of 1 or more of its employees, The exception for specified service business does not apply if the taxable income of the taxpayer is less than the sum of the threshold amount plus $50,000 ($100k MFJ)

HOWEVER - only the applicable % of qualified items of income, gain, deduction, or loss and the W-2 wages and unadjusted basis of property allocable to the business shall be taken into account

The applicable percentage means, with respect to any taxable year

100% reduced (not below zero) by the percentage equal to the ratio of (i) taxable income of the taxpayer in excess of the threshold, bears to (ii) $50,000 ($100k MFJ)

REGULATIONS ARE NEEDED

Do you include wages paid to an owner or guaranteed payments to partners in determining qualified business income?

Section 461 Limitation on Excess Business Losses

For 2018 to 2025 – 461j (relating to limitation on excess farm losses of certain taxpayers) shall not apply, and
Any excess business loss of the taxpayer for the taxable year shall not be allowed.

Any loss disallowed will be treated as a net operating loss carryover to the following taxable year.

Excess business loss means the excess of the aggregate deductions attributable to trades or businesses of the taxpayer over the sum of the aggregate gross income or gain attributable to such trades or businesses, plus $250,000 (200% of such amount in the case of a joint return)

So on a joint return, if expenses exceed income by $500,000 the excess will not be allowed in the current year.

Excess business loss for partnership or S corporation

In the case of a partnership or S corp, the limitation is applied at the partner or shareholder level, and each partner's or shareholder's share of the items of income, gain, deduction or loss shall be taken into account by the partner or shareholder in applying this section to the taxable year of such partner or shareholder with or within which the taxable year of the partnership or S corporation ends.

TAX BENEFITS FOR FAMILIES AND INDIVIDUALS

The standard deduction is increased.

For 2017 the standard deduction was $6,350 for an individual and $12,700 for MFJ

For 2018 the standard deductions will be doubled. After that, they will be inflation adjusted.

CHILD TAX CREDIT

Doubled from $1,000 to $2,000 maximum per child.

Can be phased out depending on income.

For dependent children who are younger than 17 years old at the end of the year.

The refundable portion is limited to $1,400 per child.

Partial credit is allowed for certain other dependents.

There is a nonrefundable credit of $500 available as a “family credit” for elderly dependents.

For the child tax credit, no credit will be allowed unless the child has a social security number.

INCREASED LIMITATION FOR CHARITABLE CONTRIBUTIONS

The previous limitation was 50% of adjusted gross income.

The new limit is 60% of adjusted gross income.

Excess contributions can be carried forward for 5 years.

DEDUCTIONS FOR MEDICAL EXPENSES

The itemized deduction for medical expenses had to exceed 10% of adjusted gross income before it could be deducted.

Under the new law, for 2017 and 2018 the expenses only have to exceed 7.5% of adjusted gross income before they can be deducted. This is one of the few retroactive provisions in the law.

STUDENT LOANS THAT ARE DISCHARGED ON ACCOUNT OF DEATH OR DISABILITY

Gross income does not include any amount which would be includible in gross income for the taxable year by reasons of the discharge (in whole or in part) of a student loan or a private education loan (as defined in section 140(7) of the Consumer Credit Protection Act)

SECTION 529 PLAN – ACCOUNT FUNDING FOR ELEMENTARY AND SECONDARY EDUCATION

529 plans are a way to put money away for college. Earnings on the investment grow tax free and distributions used for higher education are not taxable.

Under the new tax law, you can use up to $10,000 per year for elementary and secondary education. You can also purchase "computer technology or equipment"

PERSONAL EXEMPTIONS

This is one of the negative provisions of the new tax law.

Starting in 2018 the personal exemption amount (which was $4,050 per person in 2017) will be ZERO.

A family of four will lose $16,200 in personal exemptions starting in 2018.

STATE AND LOCAL TAX DEDUCTION

Another negative provision. State and local taxes are an itemized deduction, and were not limited.

For 2018 to 2025, the maximum deduction is $10,000 per year.

DEDUCTION FOR QUALIFIED RESIDENCE INTEREST

This is an itemized deduction (mortgage interest).

Under the new law, the maximum loan amount for which you can claim an interest deduction is $750,000. It used to be $1 million.

There will be no deduction for home equity indebtedness.

MISCELLANEOUS ITEMIZED DEDUCTIONS

For 2018 to 2025 there will not be any miscellaneous itemized deductions allowed.

These were unreimbursed employee business expenses, union dues, tax preparation fees, safety deposit box rental, job hunting expenses, and a few other items.

MOVING EXPENSE DEDUCTION

Another negative provision.

The deduction, which was on page 1 of the return, is suspended for 2018 to 2025.

ALIMONY

The deduction for alimony paid, which was on page 1 of the return, is repealed.

At the same time, alimony received is not taxable under the new law.

These provisions become effective in 2019.

ESTATE LIFETIME EXCLUSION

The existing law set a lifetime exclusion amount of $5 million, which was inflation adjusted.

Under the new law, the lifetime exclusion amount is $10 million.

EXTENSION OF TIME FOR RETURN OF PROPERTY SUBJECT TO LEVY

IRC section 6343(b) used to give the IRS 9 months to return of property subject to levy, if the IRS determined that property was wrongfully levied upon

The new period is 2 years.

FAILURE TO MAINTAIN HEALTH CARE COVERAGE

The shared responsibility payment for individuals failing to maintain minimum essential coverage has been eliminated.

Applies to months beginning after December 31, 2018.

ALTERNATIVE MINIMUM TAX FOR CORPORATIONS

The AMT for corporations has been eliminated.

This provision takes effect in 2018.

CORPORATION INCOME TAX RATE

Under prior law, corporate taxes were:

15% of the first $50,000 of taxable income
25% of the next $25,000
34% of the next $25,000
39% of the next $235,000
34% of the next $9,665,000

UNDER THE NEW LAW THE RATE IS 21%.

REDUCTION IN DIVIDEND RECEIVED DEDUCTION

Dividends received by one corporation from another corporation are not 100% taxable.

It used to be 70% or 80%, depending on the percentage ownership in the investee (70% for <20% owned, 80% for >20% owned

Under the new law, it is 50% or 65%, depending on the ownership interest percentage

EXPENSING DEPRECIABLE ASSETS (SECTION 179)

The dollar limitation is raised from $500,000 to $1 million.

The ability to deduct is phased out if you buy a lot of assets. The phaseout started at $2 million in acquisitions.

Under the new law, the phaseout starts at $2.5 million in acquisitions.

SECTION 179 DEDUCTION CAN NOW INCLUDE QUALIFIED REAL PROPERTY

Section 1245 property (as defined in 1245(a)(3), or

At the election of the taxpayer, qualified real property

Qualified Real Property

(1) any qualified improvement property described in section 168(e)(6), and
(2) any of the following improvements to nonresidential real property
- (A) Roofs
- (B) Heating, ventilation, and air conditioning property
- (C) Fire protection and alarm systems
- (D) Security systems

Section 168 (e)(6)

An improvement to an interior portion of a building which is nonresidential real property if such improvement is placed in service after the date such building was first placed in service

Certain improvements are not included – any improvement that is attributable to enlargement of the building, any elevator or escalator, or internal structural framework

LIMITATION FOR USING CASH METHOD ON A TAX RETURN

In general, C corporations, partnerships with a C corp partner, and tax shelters cannot use the cash method on a tax return.

There are exceptions for farming businesses, personal service corporations, and small businesses.

To qualify as a small business, your gross receipts must be less than $25 million

USE OF COMPLETED CONTRACT METHOD FOR CONTRACTORS

The percentage of completion method is the required method for tax purposes.

Under prior law, if gross receipts were less than $10 million, a contractor could use the completed contract method for tax purposes.

Under the new law, if gross receipts are less than $25 million, a contractor can use the completed contract method for tax purposes.

BONUS DEPRECIATION

For NEW assets placed in service, under existing law, there was bonus depreciation.

The bonus depreciation was 50% for 2017. It was being reduced 10% per year.

Under the new law, bonus depreciation for assets placed in service after 9/27/17 and before 1/1/2023 – the bonus depreciation is 100%

Bonus depreciation for 2023 is 80%

Bonus depreciation for 2024 is 60%

Bonus depreciation for 2025 is 40%

Bonus depreciation for 2026 is 20%

Apparently, under the new tax law, the bonus depreciation is available even if the property was purchased used.

LIMITATION ON DEPRECIATION FOR LUXURY AUTOMOBILES

Under existing law, first year depreciation on automobiles was limited to bonus depreciation of $8,000 and first year MACRS of $3,160.

Second year MACRS was limited to $5,100

Third year was limited to $3,050

All subsequent years were limited to $1,875

Under the new tax law, first year depreciation limit is increased to $10,000

Second year limit is increased to $16,000

Third year limit is increased to $9,600

All subsequent years are increased to $5,760.

LIMITATION ON DEDUCTION FOR INTEREST

(1) Deductible business interest shall not exceed the sum of
(A) business interest income,
(B) 30% of adjusted taxable income, plus
(C) floor plan financing interest.

The amount determined under (B) above can't be less than zero.

Any amount not deductible is carried forward to the next year.

The limitation on deductible interest does not apply to small businesses (those with receipts of less than $25 million.

Business interest income does not include investment income. It includes interest properly allocable to a trade or business.

For the interest limitation, trade or business does not include

(i) performing services as an employee
(ii) any electing real property trade or business
(iii) any electing farming business, or
(iv) the furnishing or sale of (a) electrical energy, water, or sewage disposal services, (b) gas or steam through a local distribution system, or (c) transportation of gas or steam by pipe line,

if the rates have been established by a state or political subdivision, by any agency of the U.S.. or by a PUC or similar body

Adjusted Taxable Income means:
Taxable income without regard to any item not properly allocable to a trade or business, any business interest or business interest income, any NOL deduction, any deduction under 199A (the 20% pass through deduction), and for tax years through 2021 any deduction for depreciation, amortization, or depletion

MODIFICATION OF NET OPERATING LOSS DEDUCTION

Under the new law, you can deduct the lesser of
(1) the aggregate NOL carryovers, plus the NOL carrybacks, or
(2) 80% of taxable income computed without regard to the NOL deduction

REPEAL OF NET OPERATING LOSS CARRYBACK; CARRYFORWARD

Under prior law, an NOL must be carried back 2 years unless you elect not to.

Under the new law, there is no more carryback.

Under the old law, NOLs could be carried forward 20 years.

Under the new law, carryforward is indefinite.

INSURANCE COMPANY LOSSES

The NOL for an insurance company, except for a life insurance company, must be carried back 2 years (unless you elect out) and can be carried forward 20 years.

SECTION 1031 EXCHANGES

The new law changes “property” to “real property” wherever property appeared.

The new law specifies that real property located outside the United States and real property located in the United States are not property of a like kind (you can’t do a 1031).

You can’t do a 1031 if the real property is held primarily for sale.

LIMITATION ON DEDUCTION BY EMPLOYERS OF EXPENSES FOR FRINGE BENEFITS

No deduction is allowed for fringe benefits that would be considered amusement, entertainment, or recreation

Only 50% of expense for meals provided on or near business premises will be allowed.

No deduction for transportation fringe benefits provided to an employee in connection with travel between residence and workplace

Qualified bicycle commuting reimbursement is still allowed.

No deduction for meals provided at the convenience of the employer.

Generally effective for 2018 and beyond, except for meals provided at the convenience of the employer, for which the date is 2026 and beyond.

The deduction for income attributable to domestic production activities is eliminated.

This deduction is found near the bottom of page 1 of a return, and primarily applies to oil and gas operations, but can also apply to manufacturing and film production.

NO DEDUCTION FOR FINES OR PENALTIES

Penalties imposed by the tax authorities have never been deductible.

The new law specifies that fines and penalties are not deductible, but amounts paid as restitution, remediation of property or amounts paid to come into compliance with any law which was violated are deductible.

No deduction is allowed for any settlement or payment related to sexual harassment or sexual abuse if such settlement or payment is subject to a nondisclosure agreement.

No deduction is allowed for attorney's fees related to such a settlement or payment.

EMPLOYER CREDIT FOR PAID FAMILY AND MEDICAL LEAVE

For purposes of Section 38 (general business credit), the paid family and medical leave credit is equal to the applicable percentage of the amount of wages paid to qualifying employees during any period in which such employees are on family and medical leave. The applicable percentage is 12.5%, increased (but not above 25%) by 0.25% for each % point by which the rate of payment exceeds 50%.

The maximum amount of leave subject to the credit with respect to any employee shall not exceed 12 weeks.

To be an eligible employer, you must have a written policy in place that grants all full time qualifying employees not less than 2 weeks of annual paid family and medical leave, and the rate of payment under the program is not less than 50% of the wages normally paid to such employee.

QUESTIONS

Questions

A person receives $500,000 for the sale of a CNMI real property and $5,000 is paid in as an Earnings tax deposit.

Q: How do you report this on a 1040?

A: If this is a sale of a real property, it is a capital transaction reported on Schedule D. There may be gain or loss, and the transaction may be short term or long term. The $5,000 paid in goes in the earnings tax section as a payment.

Questions

Box 1 of W-2 CM shows $24,954. Bos 12a shows $1,313 with code D. Box 16 shows $26,268.

Q: Is the $1,313 subject to Wage and Salary Tax?

A: For a CNMI government or Federal government employee, NO. For all others, YES.

Filing deadlines

W-2 forms – January 31 to IRS and to employees

Fincen 114 – April 15 online
Used to be due in June
6 month extension available

S Corporation – Still March 15

Filing deadlines

C corporation – April 15
5 month extension available

Partnership/LLC –March 15
6 month extension available

Health Insurance Coverage

Form 1095-A 1095-B 1095-C

You should have health insurance coverage but the Affordable Care Act is not relevant in the CNMI

Additional child tax credit

Cannot claim if you are taking a foreign earned income exclusion

Identity protection pin

Assigned by IRS if you were a victim of identity theft

If you don’t have a pin, leave the spaces blank on the return

RECORDS RETENTION

- 3 years are always open
  6 years are open if you don't report income and it is more than 25% of your gross
  All years are open if there is fraud or if you didn't file
  You must file for a refund within 3 years of FILING or 2 years after the tax was paid, whichever is later

FILING STATUS

SPOUSE PASSES AWAY DURING THE YEAR

MARRIED FILING JOINT FOR THE YEAR OF DEATH

QUALIFYING WIDOW(ER) WITH DEPENDENT CHILD – FOR 2 YEARS AFTER DEATH

HEAD OF HOUSEHOLD
UNMARRIED
PAID MORE THAN HALF THE COST OF KEEPING UP A HOME
QUALIFYING PERSON LIVE WITH YOU MORE THAN HALF THE YEAR

QUALIFYING PERSON

CHILD WHO IS SINGLE OR MARRIED AND YOU CAN CLAIM AN EXEMPTION

PARENT AND YOU CAN CLAIM AN EXEMPTION – YOUR FATHER AND MOTHER DO NOT HAVE TO LIVE WITH YOU

GRANDPARENT OR SIBLING WHO LIVED WITH YOU MORE THAN HALF THE YEAR AND YOU CAN CLAIM AN EXEMPTION

Personal exemptions for 2017
$4,050 per person

PHASE OUT FOR HIGHER INCOME TAXPAYERS

Claiming Dependents

Qualifying Child
Qualifying Relative

In either case – must be a citizen or resident
They cannot be a dependent of another person
They cannot file a joint return with another person

Claiming Dependents

Qualifying Child – Child, stepchild, foster child, sibling
Under age 19, or full time student under age 24
Must live with you more than ½ year
Must provide more than ½ support
You are the only one claiming them

Claiming Dependents

Qualifying Relative – Parents, grandparents, siblings

Must live with you (unless excepted see Pub. 501)

Must have less than $4,050 income

Must provide more than ½ support

You are the only one claiming them

STANDARD DEDUCTIONS FOR 2017

Single	$6,350
Married filing joint	$12,700
Married filing separate	$6,350
Head of household	$9,350

If you are single and your total income is less than $10,400 you do not have to file a return

On a married filing joint return, the amount is $20,800

You should file if there was withholding

FaTCA

FOREIGN ACCOUNT TAX COMPLIANCE ACT

Fincen 114 – ELECTRONIC Filing
Due April 15

Form 8938 – FILE WITH RETURN

REPORTING FINANCIAL ACCOUNTS IN FOREIGN COUNTRIES

FATCA – Passed in 2010. Applies to U.S. citizens, residents, and a limited number of nonresident individuals

Applies to specified foreign assets:

Foreign bank accounts

Foreign stocks not held in a financial account

Foreign partnership interests

Foreign mutual funds

Foreign issued life insurance or annuity contract with a cash value

FinCEN Form 114 (FBAR)

Report of Foreign Bank and Financial Accounts

Required if account goes over $10,000 at any time during the year

Must report the maximum value of the account during the year

Must be filed by April 15 with the IRS

Must be filed electronically

Penalty for not filing is up to $10,000 (not willful), $100,000 or 50% of account balance (willful)

FORM 8938

Total value over $75,000 during the year or more than $50,000 at end of year

Higher limit if you live abroad

$200k at year end or $300k during

$400k at year end or $600k during

Currently applies only to individuals

QUALIFIED DIVIDENDS

ORDINARY DIVIDENDS ARE TAXED AT REGULAR RATES

QUALIFIED DIVIDENDS ARE TAXED AT 0%, 15% OR 20%

0% for 10% or 15% bracket

15% for 25% to 35% bracket

MUST HAVE HELD THE STOCK FOR AT LEAST 60 DAYS DURING THE 121 DAY PERIOD THAT BEGINS 60 DAYS BEFORE THE EX-DIVIDEND DATE

Foreign taxpayers

Resident alien taxed just like a U.S. citizen – worldwide income

Nonresident alien only taxed on U.S. (in our case CNMI) sourced income

Use Form 1040-NR

Foreign earned income exclusion

Maximum deduction is $102,100

Use form 2555

Foreign tax credit is affected by excluded income

THE MAXIMUM TAX RATE IS STILL 39.6%

ADDITIONAL MEDICARE SURTAX ON LESSER OF INVESTMENT INCOME OR MODIFIED AGI - $200K SINGLE AND $250K MFJ

ADDITIONAL MEDICARE PAYROLL TAX OF 0.9 PERCENT ON EARNED INCOME - $200K SINGLE AND $250K MFJ

ADDITIONAL MEDICARE TAXES

- THERE IS A 0.9% ADDITIONAL MEDICARE TAX
- APPLIES TO MEDICARE WAGES AND SELF-EMPLOYMENT INCOME
- APPLIES TO TOTAL WAGES, AND A MARRIED COUPLE IS TREATED AS ONE "TAXPAYER" FOR THIS PURPOSE
- APPLIES TO WAGES ABOVE $200K FOR SINGLE OR HOH AND $250K FOR MFJ
- THERE IS NO EMPLOYER PORTION, BUT EMPLOYER MUST WITHHOLD
- EMPLOYEE IS ULTIMATELY RESPONSIBLE FOR THE TAX

Additional Investment Income Tax

THE ADDITIONAL 3.8% TAX DOES NOT APPLY TO NONRESIDENT ALIENS OR TRUSTS IN WHICH ALL OF THE UNEXPIRED INTERESTS ARE DEVOTED TO THE CHARITABLE PURPOSES DESCRIBED IN IRC §170(c)(2)(B)

RENTS ARE INCLUDED IN THE DEFINITION OF INVESTMENT INCOME, BUT RENTS THAT ARE PART OF A TRADE OR BUSINESS ARE NOT INCLUDED.

RENTS RECEIVED BY A REAL ESTATE PROFESSIONAL ARE TRADE OR BUSINESS INCOME

NET INVESTMENT INCOME DEFINITION

GROSS INTEREST, DIVIDENDS, ANNUITIES, ROYALTIES, RENTS

GROSS INCOME FROM TRADE OR BUSINESS IF IT IS A PASSIVE ACTIVITY OR

BUSINESS TRADING IN FINANCIAL INSTRUMENTS OR COMMODITIES

NET GAIN ATTRIBUTABLE TO DISPOSITION OF PROPERTY

REDUCED BY ANY ALLOWABLE DEDUCTIONS PROPERLY ALLOCABLE

CERTAIN ITEMIZED DEDUCTIONS ARE NOT PHASED OUT

MEDICAL EXPENSES

INVESTMENT INTEREST EXPENSE

CASUALTY OR THEFT LOSSES

GAMBLING LOSSES

401K DEDUCTION LIMIT

$18,000 DEFERRAL
$6,000 CATCH UP 50 AND OLDER

Contribution limit for SEP IRA increased to $54,000 in 2017

Also applies to solo 401k plans

Simple IRA contribution limit is $12,500 in 2017 plus $3,000 catch up

IRA ROLLOVERS

YOU ARE ALLOWED ONLY ONE ROLLOVER PER 12 MONTHS

ROLLOVERS ARE TAX FREE IF PUT INTO ANOTHER IRA OR REDEPOSITED WITHIN 60 DAYS

ESTATE TAXES

$5,000,000 LIFETIME EXEMPTION

TAX RATE IS 40% ABOVE $5,000,000

EFFECTIVELY, THE FIRST DOLLAR OF ESTATE TAX WILL BE AT 40%

THE LIMIT IS INFLATION ADJUSTED, SO FOR 2017 IT IS $5.49 MILLION FOR A SINGLE PERSON, $10.98 MILLION FOR MARRIED COUPLE

CAPITAL GAINS TAX RATE

0% If you are in 10% or 15% tax bracket

15% if you are in 25% to 35% bracket

20% if you are in 39.6% bracket

When you calculate the tax, you do get the 0% and 15% portions shown above

SOME CREDITS THAT WERE EXTENDED TO 2017

AMERICAN OPPORTUNITY TAX CREDIT – AN EXPANDED HOPE CREDIT

CHILD TAX CREDIT

EARNED INCOME TAX CREDIT

TAX FREE IRA DISTRIBUTION FOR CHARITABLE PURPOSES

IRA OWNERS WHO TAKE A DISTRIBUTION AND GIVE THE MONEY TO CHARITY DO NOT HAVE TO TREAT THE DISTRIBUTION AS TAXABLE INCOME

SECTION 179 DEDUCTION

- MAXIMUM AMOUNT THAT CAN BE DEDUCTED IS $500,000 FOR 2017
- COMPUTER SOFTWARE QUALIFIES FOR SECTION 179 DEDUCTION
- TAXPAYER CAN REVOKE SECTION 179 ELECTION ON AMENDED RETURN

Can be for new or used property

Cannot create or increase a loss

BONUS DEPRECIATION

- THE 50% BONUS DEPRECIATION DEDUCTION IS EXTENDED FOR ASSETS PLACED IN SERVICE IN 2017

- BONUS DEPRECIATION IS IN EFFECT UNTIL 2019, BUT THE 50% RATE WAS GOING DOWN TO 40% IN 2018 AND 30% IN 2019 – CHANGED BY NEW TAX LAW

- TAXPAYERS CAN ELECT TO ACCELERATE AMT CREDITS IN LIEU OF BONUS DEPRECIATION

EMPLOYEE VS. INDEPENDENT CONTRACTOR

- IF THE EMPLOYER CONTROLS ONLY THE RESULT OF THE WORK AND NOT HOW IT WILL BE DONE

WHAT IS A REAL ESTATE PROFESSIONAL?

MORE THAN 50% OF THE PERSONAL SERVICES PROVIDED BY THE TAXPAYER AND MORE THAN 750 HOURS PER YEAR MUST BE PERFORMED IN REAL PROPERTY BUSINESSES IN WHICH THE TAXPAYER MATERIALLY PARTICIPATES

IF RETURN IS MFJ, ONE SPOUSE MUST MEET THE REQUIREMENT ABOVE

A REAL PROPERTY TRADE OR BUSINESS IS ANY REAL PROPERTY DEVELOPMENT, REDEVELOPMENT, CONSTRUCTION, RECONSTRUCTION, ACQUISTION, CONVERSION, RENTAL, OPERATION, MANAGEMENT, OR LEASING, OR BROKERAGE TRADE OR BUSINESS

CREDIT FOR RESIDENTIAL ENERGY PROPERTY

30% Credit is extended through 2019

Reduced to 26% in 2020

Reduced to 22% in 2021

PROVISIONS EXPIRING IN 2017

AMERICAN OPPORTUNITY TAX CREDIT

FOR THE CHILD CREDIT – REDUCE THE EARNINGS THRESHHOLD FROM $10,000 TO $3,000 FOR THE REFUNDABLE PORTION OF THE CREDIT

Partnership income is subject to self-employment tax

LLC income is subject to self employment tax

No self employment tax if limited partner (except guaranteed payments or salary)

Guaranteed payments to partners

Payments to partners regardless of the profit or loss of the partnership

Generally subject to self-employment tax

Convert C corporation to S corporation – form/deadline

C corp NOL

Built in gains

5 year period

Allocation of income

C corporation, dividend based on shares owned

S corporation, based on shares

Partnership or llc, whatever the owners decide

Withholding at source

Types of income - FDAP

Rate

Treaties

Withholding at source

Interest
Dividends
Rents
Royalties

Does not apply to services

Flat rate of tax of 30%

BGRT applies

BGRT credit and rebate

Recipient files at the end of their tax year

Tax on transfer of real property interest in the CNMI

4CMC§1823 states

“(a) *In General*. In the case of any transfer of a CNMI real property interest, the tax imposed by section 1301 or 1202 of this Division, on the gross revenue of a transferor of such an interest shall be collected by the transferee as follows. The transferee shall deduct and withhold the tax for the account of the transferor upon every payment of money or other consideration to be made to the transferor. The amount to be deducted and withheld shall be equal to the tax imposed by section 1301 of this Division on every such payment of money or other consideration. The transferee shall deduct and withhold said amount before any payment of money or other consideration is made to the transferor, and the transferee shall report and remit the withheld tax to the Secretary as provided below.

S CORPORATIONS AND COMPENSATION TO OWNERS

Reasonable compensation must be paid

Flow through of profits without self-employment tax

LIMITED LIABILITY COMPANIES AND ELECTIONS

If no election – use form 1065 as a partnership

Can elect to be taxed as a C corporation – Form 8832

Can elect to be taxed as an S corporation – Form 2553

CONSOLIDATED TAX RETURN FILING

Can be done if one corporation owns 80% or more of another corporation

GRADUATED TAX RATE ALLOCATION

Must be allocated among a controlled group of companies

Use Schedule O for Form 1120

DIVIDENDS RECEIVED DEDUCTION

Applies to corporations that own a part of another corporation

70% if less than 20% owned

80% if owned 20% to 80%

100% if owned more than 80% or a wholly owned foreign subsidiary

SCHEDULE M-3

Used to reconcile income per books with income per tax return

For corporations with assets of $10 million or more

If you use M-3, do not use M-1

One column for temporary differences and one for permanent differences

CNMI RESIDENCY REQUIREMENTS

Physical Presence

Tax Home

Closer Connection – 11 items

INCOME SOURCING RULES

Personal Services

Interest, Dividends, Rents, Royalties

Capital Gains

Social Security

Pensions and IRA/401k accounts

INDIVIDUAL DEVELOPMENTS

IRA DISTRIBUTION UNDER AGE 59 ½ GENERALLY SUBJECT TO PENALTY

CAN USE SUBSTANTIALLY EQUAL PERIODIC PAYMENTS TO AVOID PENALTY

PAYMENTS MUST CONTINUE FOR THE GREATER OF 5 YEARS OR THE PERIOD UNTIL THE TAXPAYER REACHES AGE 59 ½

IF PAYMENTS ARE NOT MADE FOR A YEAR, OR PAYMENTS ARE MODIFIED, THE TAXPAYER OWES EARLY DISTRIBUTION TAX PLUS INTEREST BACK TO WHEN IT WOULD FIRST HAVE APPLIED

INDIVIDUAL DEVELOPMENTS

Losses from sole proprietorship

Must show profit 3 out of 5 years

To demonstrate profit motive, 9 factors are considered

1. The manner in which you conduct the activity
2. The expertise of the taxpayer or advisers
3. Time and effort expended
4. Expectation that assets used may increase in value
5. Success in other similar or dissimilar activities
6. History of income or loss for the activity
7. Amount of occasional profits earned
8. Financial status of the taxpayer
9. Whether elements of personal pleasure or recreation are involved

INDIVIDUAL DEVELOPMENTS

Safe harbor deduction for home office

Taxpayers can deduct $5 per square foot for up to 300 square feet – total of $1,500

Limited to the amount of income from the business before the home office deduction

Any excess cannot be carried forward

Excess from prior years cannot be used at the same time

May still claim full deduction for mortgage interest and taxes on schedule A if you use safe harbor

INDIVIDUAL DEVELOPMENTS

1031 EXCHANGE

45 day identification, 180 day closing

CNMI PROPERTY FOR GUAM OR U.S. PROPERTY

DEFERRAL OF GAIN

CARRYOVER OF BASIS

WHAT ABOUT WITHHOLDING?

Business DEVELOPMENTS

MAXIMUM FOR SELF-EMPLOYMENT FOR SOCIAL SECURITY IS $127,200 FOR 2017 – up from $118,500 for 2016

STANDARD MILEAGE RATE IS 53.5 CENTS PER MILE, down from 54 cents in 2016

17 cents per mile for medical or moving, down from 19 cents in 2016

14 cents per mile for charitable purposes

Foreign Trust – Form 3520

GUAM AND CNMI TRUSTS

FORM 1041

FORM 3520 SIMILAR TO FINCEN 114 OR 8938

ITIN and Form W-7

W-7 CM

Foreign taxpayer with U.S. (CNMI) filing obligation

IRS first, then CNMI

Form 1120-F

Branch Profits Tax

Branch Level Interest Tax

Schedule H

Per Diem Rates

Self-employed and Partners

Meals only, not lodging

State Dept website for rates

Fringe Benefits
Generally taxable - included on a W-2 unless it is excludable

Cafeteria plan – accident and health benefits, adoption assistance, dependent care assistance, group term life insurance, HSA

- Q: In the case of any transfer of a CNMI Real Property Interest-
- a) What is the responsibility of the Transferor to CNMI Revenue?
- b) What is the responsibility of the Transferre to CNMI Revenue?
- c) What is Payment Deposit Form 1823? What is the basis?
- d) What is the Form 1099-S relation to the above?
- A:
- (a) Transferor must report the sale of the property on tax return and takes credit for taxes paid in by transferee

- Q: In the case of any transfer of a CNMI Real Property Interest-
- b) What is the responsibility of the Transferre to CNMI Revenue?
- c) What is Payment Deposit Form 1823? What is the basis?
- d) What is the Form 1099-S relation to the above?
- A:
- (b) The transferee must withhold from the agreed upon price an amount calculated from the BGRT table. Note that it is NOT BGRT – just using the BGRT rate. The money must be remitted to the CNMI Treasury within 10 days.
- (c) The amount withheld is remitted using form 1823.
- (d) Form 1099-S is used to report the sale of real property. It will be given to CNMI Rev/Tax usually by the title company. A copy will be issued to the seller.