HOW ABOUT THAT 20 PERCENT BREAK THEY MENTIONED?

TAX PREP: TRICKIER THIS YEAR, BUT OUTCOME SHOULD BE POSITIVE FOR MANY TEACHERS

By David Gould, *Staff Editor*

Reports of major tax reform in the making came hot and heavy in late 2017. Anyone with a decent income was paying heed as Congress vowed to ratchet up their take-home compensation. Conclusive evidence on that point will have to wait until federal returns get figured and filed. That's due to the intricacies of the 2017 Tax Cuts and Jobs Act (TCJA), which are certainly plentiful and too granular to permit blanket generalities.

Having said that, news arrived last month about a major update to what TCJA is all about. It concerns small business owners and the so-called "pass-through" form of business revenue. In this 182-page clarification from the IRS there are long-awaited details that Proponent members and their accountants would naturally be curious about—especially given the 20 percent tax break this section of the Act promises.

Having these particulars delivered a full eight months after passage of the original law is far from ideal for those who take tax planning seriously. It's a testament, experts say, to how loosely worded and last-minute the section on pass-through companies and businesses was in the first place.

Before addressing this new information, it's worth reviewing the basics of the TCJA. That starts with a reminder that posted federal tax rates have come down. The old 15 percent bracket is now the 12 percent bracket. The next bracket above that used to carry a 25 percent rate, it's now at 22 percent. The one above that, which formerly skimmed off 28 percent, now takes 24 percent. Higher up the rate chart there is minimal change from the old percentages.

The TCJA, like any omnibus tax bill, is naturally going to "giveth and taketh away." While the chart of rates and brackets for the federal tax you pay looks friendlier, it has to be put in the blender with new changes to the rules concerning the personal exemption, the standard deduction and the child tax credit. The personal exemption, which last year was $4,050, is no longer. To make up for its elimination, lawmakers have roughly doubled the standard deduction, from $6,350 for single filers to $12,000 and from $12,700 for married couples to $24,000. Per-child credits are increased, so the sum total of rates and deductions will be positive for many if not most.

This brings us to the lip-smacking 20 percent tax deduction on owners of basically any business that isn't a corporation—this would include sole proprietorships, S-corps, LLCs, partnerships and anything else a Proponent member could be using as his or her structure. Let it be said right here that no article of this length could possibly cover this topic comprehensively. In fact, what's practical at this point is merely to lay out helpful advice on how to approach the topic with a professional tax preparer so that the two of you can talk about it sensibly and productively. And here are seven key points that will help you do that.

- **It's referred to as the "Section 199A deduction" or the "deduction for qualified business income."** Politically, this was a way for Congress to hand corporations their juicy new 21 percent tax rate—slashed from 35 percent—and not be hit with complaints from small and medium-sized businesses saying what-about-us?

- **The first data point the IRS provides on Section 199A is about income and eligibility.** The guidance notes the the relief "is generally available to eligible taxpayers whose 2018 taxable incomes fall below $315,000 for joint returns and $157,500 for other taxpayers." So, the ceiling on this benefit is at least reasonably generous.

In fact, the new law includes an explicit warning to employees who would attempt some kind of in-name-only shift, in order to enjoy the 20 percent deduction.

- **The concept of the relief is this:** Owners of pass-through businesses usually do pretty well for themselves, but they don't have corporate lawyers and accountants helping them squeeze down their tax bills. Much of their business revenue passes through and finds its way onto the owner's personal Form 1040 tax return, where it's taxed at a high rate. So, on its way "passing through" from the business P&L sheet to your personal 1040 income, 20 percent of it disappears.

- **Some writers and journalists with expertise in tax law have harshly greeted the pass-through portion of the TCJA.** Writing on the Forbes website, veteran commentator Howard Gleckman contends that the "special 20 percent individual income tax deduction for pass-through businesses such as partnerships and sole proprietorships was misguided—and probably doomed to fail—from the beginning." Looking through the August update, Gleckman notes that officials "attempt to address some of the law's most wrong-headed features but, as written, the statute probably is unfixable." So, don't be shocked if your own tax accountant seems to be at wit's end about how to interpret Section 199A, so as to (legally) leverage it to your advantage.

- **The initials "SSTB" are important to know.** They come into the conversation pretty quickly—and seemingly in a way unkind to golf professionals. SSTB stands for Specified Service Trade or Business.

- **What sounds like a prohibition against SSTBs receiving this 20 percent small-business tax break is part of the newly issue guideline report.** "Broadly speaking," the IRS material states, "an SSTB is any business involving the performance of services in health, law, 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 one or more of its employees or owners.'" One tax accountant blogging about the above paragraph concluded: "In other words, if the success of your business or practice depends on you and not on something that you sell, you could very well be left out of the deduction."

- **Not so fast—in a further clarification, instructors who don't have endorsement contracts look to be back on the good side of the dividing line.** So, if you basically look like a candidate for this 20-percent-off-the-top, but your CPA is sounding antsy about the references to "athletics" and "reputation and skill," you'll want to get geeky and point him or her toward Reg. 1.199A-5(b)(2)(xiv). That's where it says, basically, that you fit the SSTB definition for the purposes of this deduction as long as you:
  - don't get compensated for "endorsing products or services," or,
  - you don't "receive fees, compensation or other income for the use of [your] image, likeness, name, signature, voice, trademark, or any other symbols associated with the individual's identity," or,
  - lastly, you don't receive "fees, compensation, or other income for appearing at an event or on radio, television, or another media format."

Any Proponent member who would be DQ'd from the Section 199A deduction by the above probably had no shot anyway, based on earning income above $157,500.

Again, the point here is to define things well enough to prevent your discussion with a tax preparer from wandering aimlessly through unanswered questions. With any luck the points laid out above are sufficient in that regard.

One other stream of commentary sparked by the Tax Cuts and Jobs Act—made louder by these new guidelines on pass-through—is that abandoning employee status for a switchover to independent-contractor status, in order to scoop up the new deduction, is more complex than it may seem. In fact, the new law includes an explicit warning to employees who would attempt some kind of in-name-only shift, in order to enjoy the 20 percent deduction. In another article, upcoming soon, we'll discuss the longstanding 1099-versus-W2 debate in light of all these recent changes. PG