American Bankers Association

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Preliminary Review of House Tax Reform Bill

November 2, 2017

Overview
On Nov. 2, 2017, the long-awaited bill to reform the tax code was released. ABA supports comprehensive tax reform and looks forward to continuing to work with policymakers in crafting the final legislation in accordance with our core principles. The following is a brief summary of key provisions affecting banks directly or indirectly. This is based on our preliminary analysis of the bill and should be used with caution. We will continue to analyze the detailed provisions.

Business Tax Rates
C corporations: 20 percent rate
Effective date: Jan. 1, 2018
Transition rules: none

Pass-throughs: 25 percent rate
The 25 percent rate applies to passive shareholder income. For active shareholders, there are restrictions as to the application of the rate between compensation and business income. Generally, the restrictions are based on two alternatives: a 70/30 split (compensation/business income) or an alternative test based a "capital percentage."
Effective date: Jan. 1, 2018
Transition rules: none

Interest Expense
Deductions for net business interest expense will be restricted. Note that the restriction is for net business interest expense, so banks as taxpayers should not be affected by this restriction. For businesses with gross receipts of $25 million or less, there will be no restriction. For other business taxpayers, the limitation will be based on the amount that net business interest expense exceeds 30 percent of adjusted income.
Effective date: Jan. 1, 2018
Transition rules: none

Tax Credits
The research and development and low income housing credits will be continued. Generally, credits (including new markets, historic) are eliminated. Energy credits continue their scheduled phase-out with certain modifications.
Effective date: Jan. 1, 2018
Transition rules: Credits will continue to be available for investments and commitments made prior to the effective date.

Capital Expensing
The plan includes 100 percent expensing for all non-real property capital expenditures made from Sept. 27, 2017 through 2022. After five years, existing provisions with 50 percent expensing and Section 179 apparently will be restored.
Effective date: Jan. 1, 2018
Transition rules: Applies to capital expenditures placed in service on or after the effective date.

Net Operating Losses
Net operating loss carrybacks are eliminated. Carryforward of net operating losses appear to be allowed an indefinite life, subject to a 90 percent limitation.
Effective date: Losses generated Jan. 1, 2018, or later.
Transition rules: Existing carryforwards at Jan. 1, 2018, appear to be subject to existing rules.

FDIC Premiums
The deduction for FDIC premiums is eliminated for banks with assets of over $50 billion. For banks with assets of between $10 billion and $50 billion, the deduction is eliminated proportionately as the size of the bank approaches $50 billion.
Effective date: For premiums paid after Jan. 1, 2018
Transition rules: none

Credit Unions and Farm Credit System
Unfortunately, the bill does not address the historic inequality of taxation between business entities providing the same services.

International Taxation
The bill provides for the establishment of a territorial system of international taxation. To address base erosion concerns, a variety of provisions are proposed, including potential restrictions on interest expense and alleged earnings shifting. For previously untaxed deferred foreign income, there is a deemed repatriation and taxable event. There is a two-tier tax rate structure: 12 percent for taxpayers with cash and cash equivalents and 5 percent for taxpayers with earnings invested in property, plant and equipment.
Effective date and transition rules: Territorial system applies to taxable years beginning on or after Jan. 1, 2018. Deemed repatriation occurs in taxable year ending Dec. 31, 2017. Tax may be deferred over eight years with a slightly higher rate.

Other Issues of Particular Concern to Banks
BOLI / COLI: no apparent change
Municipal securities: no apparent change, with the exception of new rules for private activity bonds
Mark-to-market: no apparent change
Information reporting pay-fors: no known provisions

Other Provisions

- Sets individual brackets of 12, 25, 35 and 39.6 percent. Top rate applies to AGI (MFJ) of $1 million or more
- Doubles standard deductions; eliminates of personal exemptions; expands child credits
- Retains mortgage interest (subject to $500,000 cap, down from $1 million), charitable and property tax deductions; eliminates state income tax deduction
- Eliminates AMT starting after 2017. AMT credit carryforwards may be refunded at 50 percent in later tax years.
- Doubles estate tax applicable exclusion amount to $10 million, indexed for inflation, starting after 2017. Repeals estate and generation-skipping transfer tax after 2023, while maintaining stepped-up basis in estate property.
- Substantially retains retirement savings benefits; lowers from 62 to 59½ the age at which employees may take in-service distributions from defined contribution plans and liberalizes hardship withdrawals and loans.
- Retains capital gains, dividend and interest income beneficial rates