U.S. Tax reform considerations

Accounting methods and credit services (AMCS)

On December 22, 2017, the president signed into law H.R. 1 (originally known as the Tax Cuts and Jobs Act), the most wide-ranging reform to the Internal Revenue Code in over 30 years. The new tax law reduced the corporate tax rate and has had an immediate impact on income and expense recognition, cost recovery, and credits.

**Corporate tax rate reduction**

The corporate tax rate was reduced from 35 percent to 21 percent, generally effective January 1, 2018.

**AMCS considerations:**

— The reduction in tax rate presents a one-time transition opportunity for a permanent benefit through traditional tax accounting method changes.

— Caution: The reduced tax rate affects deferred tax assets and liabilities on corporate balance sheets and could result in a significant write-down.

**Income inclusion**

Section 451 was modified to require accrual method companies to recognize income for tax purposes no later than the year in which the revenue is recognized for book purposes.

**AMCS considerations:**

— Companies should consider doing a “methods scrub” to identify tax accounting methods that may be affected and thus require a method change.

— Consider how revised section 451 interacts with the financial accounting standards for customer revenue (ASC 606).

**Increased expensing**

Bonus depreciation is increased from 50 percent to 100 percent for qualified depreciable property and applies to original and used property acquired after September 27, 2017 and before 2023 (phase-out between 2023 and 2026).

**AMCS considerations:**

— The ability to fully expense qualified new and used property significantly increases the potential benefits of cost segregation and construction tax planning studies.

— Companies in acquisition mode should review structuring deals as actual or deemed asset acquisitions to permit current expensing for qualified property.

**International taxation system**

There were fundamental changes to the taxation of multinational entities, including a one-time mandatory repatriation of accumulated foreign earnings and profits (E&P) and the new Base Erosion and Anti-Abuse Tax (BEAT).

**AMCS considerations:**

— E&P planning includes working with international tax professionals to analyze classification of the 15.5 percent rate for cash and cash equivalents versus the 8 percent rate for illiquid assets.

— BEAT planning includes evaluating allowed vs. allowable deductions, what constitutes costs of goods sold, modeling bonus depreciation and other methods for related foreign party capital purchases, and evaluating how the research and development (R&D) tax credit and applicable section 38 credits can reduce the amount of BEAT that gets imposed.
Repeal of section 199

The domestic production activities deduction (DPAD) under section 199 was repealed for tax years beginning after December 31, 2017.

AMCS considerations:

— Companies that claimed the DPAD on prior year returns, as well as companies that did not because their taxable income was limited, should analyze their section 199 positions for all open tax years in which they have taxable income.

— An opportunity may exist for companies to maximize their DPAD in 2017 due to mandatory repatriation, which will generally result in an overall taxable income increase in 2017.

Other considerations

Below are several other aspects of the new tax law to consider.

— Repeal of election to accelerate alternative minimum tax (AMT) credits in lieu of bonus depreciation

— Significant contraction of section 118, contributions to capital

— Capitalization and amortization of research and experimental (R&E) expenses after 2021 (including software development)

— Limitations on deductions for entertainment and fringe benefits

— Repeal of deduction for local lobbying activities

— Limitations on the deduction for net business interest expense

— New employer credit for paid family and medical leave

— Qualified opportunity zone gain deferral provision

— Modified rehabilitation credit

— Limitations on the use of net operating losses (NOL).

Why KPMG?

KPMG’s AMCS practice has in-depth knowledge of accounting methods, fixed assets, and business credits and incentives. AMCS works closely with other service lines, as well as Washington National Tax, to help companies in all industries assess and address the implications of tax reform.

R&D tax credit

The new tax law did not directly affect the R&D tax credit; however, companies should evaluate the following incidental considerations.

Increases net credit:

With the lower 21 percent tax rate, the “net” R&D tax credit benefit increased from 65 percent to 79 percent.

Reduces tax liability:

With corporate AMT repeal and the addition of new international provisions, more corporations need R&D credits to reduce their tax liability.

Adds value for pass-through owners:

With higher exemptions for personal AMT, more pass-through owners will benefit from the R&D credit.

Offsets NOLs:

Post-2017, NOLs can only offset 80 percent of taxable income, increasing the value of R&D credits as an offset to some or all of the tax on the remaining 20 percent.


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