

Planning Considerations for Specified Services Businesses A Note on 2018 Federal Tax Reform

How Does the New 20% Deduction on Taxable Profit Apply to Specified Service Businesses?

Owner's Taxable Income, Including Salary and Taxable Profit from Specified Service Business (LLC and "S" Corp.)	Can Owner Be Eligible for New 20% Deduction on Taxable Profit From Specified Service Business? (SALARY FROM BUSINESS IS NOT ELIGIBLE FOR 20% DEDUCTION)
Up to \$315,000 total taxable income for married filing joint owners	Yes (20% deduction may be limited based on certain thresholds)
Up to \$157,500 total taxable income for single filing owners	Yes (20% deduction may be limited based on certain thresholds)
\$315,000 - \$415,000 total taxable income for married filing joint owners	Partially (20% deduction will be "phased out" in this income range)
\$157,500 - \$207,500 total taxable income for single filing owners	Partially (20% deduction will be "phased out" in this income range)
More than \$415,000 total taxable income for married filing joint owners	No
More than \$207,500 total taxable income for single filing owners	No

Planning for Specified Services Business When Owner's Total Taxable Income is Less than \$415,000:

- Should the structure of owner's salary/guaranteed payments be reviewed to determine reasonable compensation for services performed?
- Should any self-rental arrangements for office space be reviewed to determine fair market value for lease rate being paid?
- Have the advantages/disadvantages of LLC vs. "S" corporation organization structure been considered?

Please Note:

- ✓ Under the law as currently passed, LLC could be more advantageous than "S" Corporation in allowing greater portion of taxable profit from business to be eligible for new 20% deduction.
- ✓ For business currently organized as "S" corporation, converting to an LLC likely requires liquidation of the corporation, possible taxable event to shareholders and formation of new legal entity.
- ✓ Possible alternative for business currently organized as "S" corporation -- could new LLC entity/entities be established to contract with the corporation for services performed by the owners?

Other Planning for All Specified Services Businesses:

- Does the business have more than one revenue stream? Can activities of the business be evaluated for segregation into specified services, non-specified services and other revenue sources (this may not require establishing a separate entity)?
- If business has goal to reinvest significant net profits for growth of operations, expansion of service capabilities, expansion of geographic reach, etc. and maximize value for eventual sale, have advantages of a "C" corporation organization structure been considered (lower corporate tax rate on reinvested profits)?

Next Steps:

Please contact your Baratz representative to discuss your individual situation. We will offer detailed analyses of companies to determine how to optimize salaries, rents, depreciation and other components in order to maximize the benefits of the reforms. This additional service will be assessed on an individual basis. We look forward to working with you.