Highlighting the Key Differences in the Treatment of Farmers and Small Business Owners Between the U.S. Senate and House Tax Reform Proposals

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On November 9th, the House of Representatives' Ways and Means Committee approved its version of the Tax Cuts and Jobs Act, the current tax reform legislation being debated at the federal level. The amended bill released from the Committee included only minor changes from the farming and small business perspective as compared to the original bill introduced into the Committee last week.

On the same day, Senate Republicans unveiled their own version of the Tax Cuts and Jobs Act, which contrasts with the House version in the following areas relevant to agriculture and other small businesses:

The Senate plan proposes to retain seven tax brackets for individuals, ranging from a bottom rate of 10% to a top rate of 38.5%, and this top 38.5% rate would only apply when taxable income exceeds $500,000 for single filers (and $1,000,000 for married couples filing jointly). In contrast, the House version proposes to collapse the number of individual tax brackets from seven to four, while increasing the bottom rate to 12% and maintaining the top rate at its current level of 39.6%.

The Senate plan also treats income earned by owners of pass-through entities (partnerships, LLCs, and S-Corporations) differently than the House plan. The House plan fixes a maximum 25% tax rate for certain income earned by pass-through businesses. The Senate plan does not set a maximum pass-through rate, but instead, proposes relief in the form of a 17.4% deduction for qualifying pass-through income. Under both plans, pass-through income from service-oriented businesses generally would not qualify for these reduced rates and would remain taxable at each business owner's respective individual marginal tax rates.

Both the Senate and House plans propose to reduce the corporate tax rate to a flat 20%. However, the Senate plan delays implementation of this change until 2019.

Another major difference between the two proposals involves the deduction for state and local taxes. Under current law, individuals are allowed a deduction for income and property taxes paid at the state and local level. The House bill would eliminate the deduction for state income taxes, but preserve a deduction of up to $10,000 for property taxes paid. In contrast, the Senate version would completely eliminate the state and local tax deductions altogether for individuals. As we explained in our previous article, however, neither the Senate nor House versions would change the deduction for state and local taxes (including property taxes) incurred in carrying on a trade or business like a farm.

Like the House version, the Senate plan proposes to nearly double the federal estate tax exemption amount (the value of assets an individual can pass free of tax upon death) from $5.49 million under current law to $10 million per person (indexed for inflation). However, the Senate plan does not include an eventual complete repeal of the federal estate tax as the House version does.

In addition to nearly doubling the standard deduction for all taxpayers just as the House version proposes to do, the Senate version also proposes to: (i) eliminate a current restriction on the total amount of itemized deductions that can be claimed; (ii) repeal the alternative minimum tax; (iii) loosen the cap on the amount of business-related purchases that can be immediately expensed; (iv) increase the cut-off for agricultural operations organized as C corporations to use a cash method of account; (v) limit nonrecognition of gain through like-kind exchanges to real property only; and (vi) repeal the deduction for domestic production activities.

Moving forward, the full House will take up debate and potentially vote on its version next week. The Senate Finance Committee is scheduled to internally consider its version starting next Monday, November 13.

We at Rembolt Ludtke LLP will continue to monitor and provide updates on developments in this proposed legislation as it moves through the U.S. Senate and House.

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4825-1965-9604, v. 1