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Manufacturing and Distribution

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Tax Planning

Tax Reform: What's In It for You?

Last December, with a vote of 227 to 203, the U.S. House of Representatives passed the final tax reform bill, and the Senate followed with a vote of 51 to 48. Love it or hate it, the Tax Cuts and Jobs Act represents some of the most sweeping tax changes in a generation.

The new tax law not only includes new lower tax brackets, it also includes changes to the types of deductions available, what qualifies for various deductions, and how revenues generated internationally are treated. The changes impact businesses and individual taxpayers. As with most tax legislation, the new rules will benefit some and irritate others.

Many provisions will kick in this year—effective for tax years beginning after Dec. 31, 2017—and many sunset after Dec. 31, 2026.

Here are some highlights of the overhaul.

Flat corporate rate: Beginning in 2018, corporations must pay a flat tax rate of 21 percent, down from a maximum of 35 percent—a big drop.

To put this into perspective, 21 percent is the lowest U.S. corporate tax rate in almost 80 years and is significantly lower than tax rates in China, France, Germany, Japan, and Spain. This corporate tax rate cut is not scheduled to expire.

Pass-through deduction: For owners of LLCs, partnerships, and S corporations located in the U.S., the new law provides a 20 percent deduction for profits earned by these types of pass-through entities. For taxpayers who earn above certain levels of adjusted gross income (AGI), the deduction is limited to 50 percent of the taxpayer's share of W-2 wages paid by the entity. The AGI phase-out limit starts at $315,000 for married couples filing jointly and $157,000 for single taxpayers.

Note that the deduction is generally not available for entities involved in certain types of service businesses.

Corporate AMT repealed: The law repealed the alternative minimum tax (AMT), which previously added significant complication to corporate tax compliance. The law continues to allow companies to offset regular tax liability by any minimum tax credit (MTC) they may have for any tax year. For tax years 2018 to 2020, the MTC is refundable up to 50 percent of the excess credit. In 2021, the remaining credit is allowed.

The bill also changed AMT for individual taxpayers, increasing the exemption amounts to $109,400 for married-filing-jointly taxpayers and $70,300 for single taxpayers. The bill also increased the AMT phase-out exemptions to $1 million for married taxpayers filing jointly and $500,000 for single taxpayers. Given these high numbers, much fewer individual taxpayers will be subject to AMT moving forward.

Bonus depreciation extended: For qualified property acquired and placed into service from September 28, 2017 through December 31, 2022, 100 percent first-year depreciation is available. This is a 100 percent improvement over the 2017 depreciation amount of 50 percent bonus depreciation.

This deduction is available for most new assets with a depreciable life of 20 years or less. After December 31, 2022, bonus depreciation gradually reduces through December 31, 2026. In a change from past bonus depreciation rules, used as-

Continued on page 3

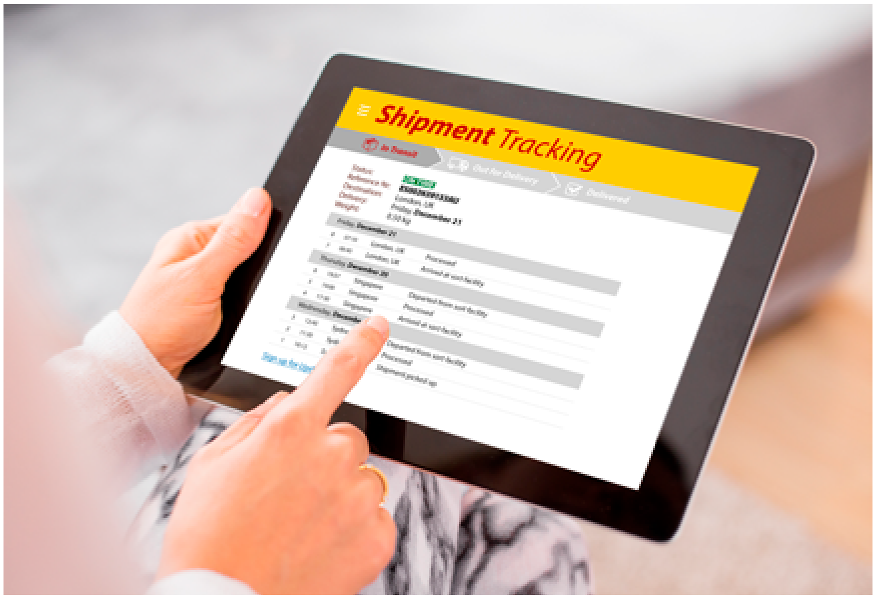
Word to the Wise

Optimizing Operations with IoT

Have you heard of the Internet of Things (IoT)? In the consumer world, IoT refers to linked online-capable devices that allow objects to be controlled remotely. These devices include such things as wireless fitness monitors, smart home technology, and self-driving cars. Experts estimate that there will be as many as 14 billion of these devices active by 2022.

The industrial IoT is also booming. Forbes reports that 71 percent of those surveyed believe IoT will significantly influence their business, with 82 percent reporting the focus will be on operational efficiency and improved product quality.

Is your company ready to exploit the power of IoT technology?



Benefits Around the Plant

It might be difficult to imagine how a wireless fitness monitor translates to a manufacturing plant. But in the same way that avid exercisers can use a fitness bracelet to track progress and sync data to their computers, progressive manufacturing and distribution executives can use IoT devices to track operational progress, increase efficiency, save money, and address operational issues.

What's involved is a network of data-gathering sensors that can communicate machine to machine, machine to person, and person to machine, capturing and analyzing data generated by equipment, systems, and people.

For example, an IoT manufacturing solution can do the following.

Track assets: With real-time, continuous visibility into the location and status of assets like parts, fixtures, tooling, and goods in transit, you can accurately identify and anticipate issues that need attention. This type of monitoring can also keep tabs on production flow to eliminate waste and excess inventory.

Monitor equipment: Regular equipment status checks minimize downtime and failure risk. IoT-enabled sensors automatically trigger alerts on variables such as temperature limits and initiate the appropriate response from maintenance immediately.

Ensure quality: IoT makes it possible to monitor items at a granular level. For example, sensors embedded in a torque wrench used in assembling a complex part can capture the precise amount of torque applied, which wrench was used, when it was last calibrated, and who last used it.

With this information, you can identify faults in real time, such as flaws in the wrench, the product, or the user's technique. Historical data can reveal patterns that might indicate production issues requiring adjustment.

Improve safety: When shop floor workers use wearable technologies, they receive real-time machine and production information to help them anticipate and resolve problems quickly, before they escalate. These devices can also be designed to detect obstacles in the path of a forklift, for example, to minimize the risk of injury.

In the Executive Office

Of course, data collection is not useful without data analysis. IoT technology must include analytics to provide a higher level of awareness and truly actionable data.

Most manufacturers and distributors find a customized dashboard to be most helpful, with all aspects of the dashboard fine-tuned to deliver the right information to the right people at the right time. This instant visibility creates a culture of managing by the minute, not by the hour, week, month, or year.

With different views available for different job titles, executives and managers get precisely the information they need to make informed, data-driven decisions.

Of course security concerns come into play with this type of technology, so any software solution must be vetted for security protocols that protect access to your company's operations.

The IoT is upon us, so now's the time to investigate how this type of automation might work for your business.

Interested in IoT plant automation? We can help you determine your next steps.

Tax Reform Impacts

Continued from page 1

sets may qualify, assuming they are new to the taxpayer.

Section 179 limitations increased: This provision allows you to expense otherwise depreciable property if placed into service in 2018. Expense and investment limitations are now increased to $1 million for fixed asset costs, with an investment limit of $2.5 million. The bill also substantially expands the definition of qualified real property eligible for Section 179 to include such items as HVAC units, windows, and roofs.

QIP changes: Qualified Improvement Property (QIP) for nonresidential property, generally defined as improvement to the interior of real property (with some requirements and exclusions) no longer qualifies for bonus depreciation. Also, QIP was previously depreciated over 39 years, but now has a 15-year life.

Interest expense deduction limited: Prior to tax reform, companies were allowed to deduct their interest expenses. However, businesses with gross receipts over $25 million are limited to a net interest expense of just 30 percent of adjusted taxable income, business interest income, and floor-plan financing interest. Controlled groups of companies with average annual gross receipts of $25 million or less (for the three-taxable-year period ending with the prior taxable year) are exempt.

Cash accounting rules expanded: Businesses can elect the cash basis of accounting, even if they hold inventory, as long as the controlled group's average gross receipts are under $25 million. This can also eliminate the requirement to include indirect and overhead expenditures in the cost of inventory (UNICAP).

No entertainment expenses: No deduction will be allowed for entertainment after Dec. 31, 2018. Meals provided for the convenience of an employer, previously deductible at 100 percent, are now deductible at 50 percent, and this deduction phases out entirely after 2025. Work-related meals are still generally deductible at the current 50 percent level.

NOL limits: Net operating losses (NOL) created in 2018 and beyond are now limited to 80 percent of taxable income. No carrybacks of net losses are allowed, but they can be carried forward indefinitely.

Tax on foreign earnings: For earnings in a foreign subsidiary, the bill imposes a mandatory "transition" tax on certain accumulated foreign earnings held in cash or illiquid assets. Foreign earnings held in cash or cash equivalents are taxed at a 15.5 percent rate, and the remaining earnings are taxed at an 8 percent rate. You can generally pay this transition tax in installments over eight years.

Previously, there was no tax imposed on foreign earnings until the earnings were repatriated.

Lower individual rates: Tax rates are 10 percent, 12 percent, 22 percent, 24 percent, 32 percent, 35 percent, and 37 percent. The top rate was previously 39.6 percent. These lower rates are scheduled to expire in 2025.

The standard deduction for couples filing jointly jumps from $13,000 to $24,000, and for single taxpayers, the standard deduction rises from $6,500 to $12,000. The personal exemption, currently at $4,150, is repealed.

State, local, and real estate taxes: Married-filing-jointly taxpayers can elect to deduct sales, income, or property taxes up to $10,000.

Charitable contribution limits: The deduction for charitable contribution jumps to 60 percent of AGI, up from 50 percent in prior years.

Estate tax exemption: The federal estate and gift tax exemption increased to $11.18 million, effective for decedents dying and gifts made after 2017.

Of course these are just a number of the changes included in the bill, with many others that might apply to your specific corporate or individual tax circumstances.

Because of the sweeping nature of the changes, tax planning is especially important this year. The law contains many underlying nuances, calculations, and deadlines that must be carefully accommodated in order to maximize the new provisions.

Let's talk taxes! We can help you plan ahead to take advantage of all the Tax Cuts and Jobs Act offers.

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Talk to Lenders About Accounting Changes

Over the past few years, the Financial Accounting Standards Board (FASB) issued new accounting standards that will have a major impact on manufacturers and distributors.

For example, ASC 606 requires a new five-step model of revenue recognition for all customer contracts and is effective for privately held companies for periods beginning after Dec. 15, 2018. ASC 842 requires that lease obligations be reported on the balance sheet for periods beginning after Dec. 15, 2019.

Both standards were designed to improve the information contained in financial statements and make them more useful for lenders, investors, and others. Both will change the way income and liabilities are reported—which may impact your banking and lending arrangements.

It is wise to proactively communicate these changes to your bank, but you won't know exactly how these standards will impact your financial statements until you actually apply them. Even so, initiating a conversation with your bankers now, with implementation dates approaching, lets them know you are on top of the new requirements and eager to have an open discussion about them.

To prepare for your conversation:

Review the standards. Both standards are extremely complicated and demand a significant amount of work up front before you can implement them. Familiarize yourself with what is required.

Start testing. Once you have determined the effect of the new standards, you can take steps to modify existing provisions. For example, relative to ASC 606, you may be able to rework your contracts to avoid a negative impact on your revenue recognition.

Educate your team. Your lenders may not be aware of how these standards will affect your financial statements. Letting them know what to expect will help avoid surprises.

Feel free to ask your CPA to accompany you to this meeting. Your accountant can help put your bankers at ease about the upcoming changes.