Strafford

FOR LIVE PROGRAM ONLY

The C-Corporation as a Viable Entity: Tax Reform Changes, Section 1202 Stock and S-Corporation Conversions

TUESDAY, MAY 21, 2019, 1:00-2:50 pm Eastern

IMPORTANT INFORMATION FOR THE LIVE PROGRAM

This program is approved for 2 CPE credit hours. To earn credit you must:

- **Participate in the program on your own computer connection (no sharing)** - if you need to register additional people, please call customer service at 1-800-926-7926 ext. 1 (or 404-881-1141 ext. 1). Strafford accepts American Express, Visa, MasterCard, Discover.
- **Listen on-line** via your computer speakers.
- **Respond to five prompts during the program plus a single verification code.**
- To earn full credit, you must remain connected for the entire program.

WHO TO CONTACT DURING THE LIVE PROGRAM

For Additional Registrations:
-Call Strafford Customer Service 1-800-926-7926 x1 (or 404-881-1141 x1)

For Assistance During the Live Program:
-On the web, use the chat box at the bottom left of the screen

If you get disconnected during the program, you can simply log in using your original instructions and PIN.

Tips for Optimal Quality

Sound Quality

When listening via your computer speakers, please note that the quality of your sound will vary depending on the speed and quality of your internet connection.

If the sound quality is not satisfactory, please e-mail sound@straffordpub.com immediately so we can address the problem.

The C-Corporation as a Viable Entity

May 21, 2019

Paul Neiffer, Principal
CliftonLarsonAllen, Yakima, Wash.
paul.neiffer@claconnect.com

Craig W. Smalley, Co-Founder / CEO
CWSEAPA, Orlando, Fla.
craig@cwseapa.com

Notice

ANY TAX ADVICE IN THIS COMMUNICATION IS NOT INTENDED OR WRITTEN BY THE SPEAKERS' FIRMS TO BE USED, AND CANNOT BE USED, BY A CLIENT OR ANY OTHER PERSON OR ENTITY FOR THE PURPOSE OF (i) AVOIDING PENALTIES THAT MAY BE IMPOSED ON ANY TAXPAYER OR (ii) PROMOTING, MARKETING OR RECOMMENDING TO ANOTHER PARTY ANY MATTERS ADDRESSED HEREIN.

You (and your employees, representatives, or agents) may disclose to any and all persons, without limitation, the tax treatment or tax structure, or both, of any transaction described in the associated materials we provide to you, including, but not limited to, any tax opinions, memoranda, or other tax analyses contained in those materials.

The information contained herein is of a general nature and based on authorities that are subject to change. Applicability of the information to specific situations should be determined through consultation with your tax adviser.

Why a C-Corporation?

What Makes C-Corporations Attractive Post TCJA?

- Flat federal tax of 21%
  - As opposed to a potential non-allowable IRC §199A deduction for pass-thru companies
- Tax-Free Health and Fringe Benefits
  - As opposed to pass-thru companies
- Improved retirement benefits
- May qualify for a IRC §1202 exclusion from capital gains tax upon exiting the C-Corp

Drawbacks to a C-Corporation

- Double taxation
- Potential state income tax issues
  - That may not have been a concern as a pass-thru
- A potential for higher FICA taxes on certain shareholders
- Disallowance of IRC §199A deduction on QBI

The Effects of Tax Reform on C-Corporation

- Outside of a flat 21% tax on C-Corporations, other benefits arise making the tax election of a C-Corporation a better choice for certain taxpayers.
  - For example, taxpayers are able to convert from a partnership or S-Corporation, to a C-Corporation tax-free. In so converting provide tax-free distributions of previously taxed income.

Revenue Procedure 2018-44

- The Tax Cuts and Jobs Act includes two changes that affect a corporation's revocation of an S election to be a C corporation:
  - The corporation should report net adjustments attributable to the revocation over six years. For more information see Revenue Procedure 2018-44.
- Distributions of cash following the post-termination transition period may be treated as coming out of the corporation's accumulated adjustments account and accumulated earnings and profits proportionally resulting in part of the distributions being non-dividend distributions from the C corporation. The non-dividend distributions may not be subject to tax at the shareholder level if the shareholder has sufficient stock basis.
- Additional guidance will be coming.

Revenue Ruling 2019-13

- When an S corporation's S status terminates, it goes through a “post-termination transition period” (PTTP) under Code Sec. 1377(b)(1). During the PTTP, the former S corporation can continue to take advantage of some of the benefits associated with its S status. For example, Code Sec. 1371(e) provides that, in general, any distribution of cash by a former S corporation with respect to its stock during the PTTP is applied against and reduces the adjusted basis of the stock to the extent the distribution does not exceed the corporation's AAA.
- Code Sec. 302(a) sets conditions for distributions in redemption of stock of a corporate shareholder being treated as distributions in payment in exchange for the stock. Where those conditions are not met, such distributions are treated as distributions of property to which Code Sec. 301 applies. Code Sec. 301 sets out rules for the treatment of such distributions, including treatment of the distributions as dividends and as amounts applied against basis.

Example

- X is a corporation that once was a C corporation and later elected to be an S corporation. X's S election terminated, such that it is now a C corporation. A, an individual, owns all 100 shares of the outstanding stock of X. X is a calendar-year taxpayer. At the time of its conversion to an S corporation, X had accumulated earnings and profits (E&P) of $600x and no current E&P. At the time of the termination of its S election, X's AAA was $800x and its accumulated E&P was still $600x. During X's PTTP, X redeems 50 of A's 100 shares of X stock for $1,000x. X makes no other distributions during the post-termination transition period. Pursuant to Code Sec. 302(d) of the Code, the redemption is characterized as a distribution subject to Code Sec. 301. For the taxable period that includes the redemption, X has current E&P of $400x.
- The Revenue Ruling provides that the corporation should reduce its AAA to the extent of the proceeds of the redemption pursuant to Code Sec. 1368. The redemption of 50 of A's 100 shares of X stock for $1,000x is characterized as a reduction of X's $800x of AAA with the remaining $200x characterized as a dividend under Code Sec. 301(c)(1).

Steps to Avoid Double Taxation

- Take “reasonable compensation” as a C-Corporation shareholder
  - Reasonable compensation for a C-Corporation is different than what it is for an S-Corporation. Defined, reasonable compensation basically boils down to what the shareholder would be paid, doing the same job, somewhere else.
  - In the real world, the reasonable compensation test is often not easy to apply to closely held companies. Shareholder-employees are often business founders who made big personal sacrifices over the years, were grossly underpaid in some years, and have been the driving force behind their company’s growth and profitability.

Steps to Avoid Double Taxation (Con't)

- Reasonable Compensation – As Per Tax Court
  - Tax Motivation Factors
    - ◊ Would a hypothetical outside investor conclude that return on shareholder equity hasn't been reduced to unacceptably low levels because of excessive compensation to shareholder-employees? Based on trends in court decisions, this so-called hypothetical outside investor standard now appears to be the single most important factor in assessing compensation reasonableness.
    - ◊ Is it clear that compensation levels aren't determined simply by percentage of stock ownership?
    - ◊ Does the company have a history of paying at least some dividends? However, the mere fact that no dividends have been paid doesn't by itself prove that compensation is unreasonable.

Steps to Avoid Double Taxation (Con't)

- Typically, fringe benefits are not deductible directly from a pass-thru company.
  - Fringe Benefits Deductible By a C-Corporation
    - ◊ Health Insurance
    - ◊ Contributions to a Health Reimbursement Account (HRA)
    - ◊ Education reimbursement of up to $5,150 per employee, per year
    - ◊ Employee Stock Options
    - ◊ Retirement Planning Services
    - ◊ Commuting Benefits
    - ◊ Dependent Care Benefits

Steps to Avoid Double Taxation (Con't)

- Other potential deductions for a C-Corporations
  - Paying wages to family members, such a children for services performed, provided those services and resulting pay are reasonable.
    - ◊ When paying children, taxpayer's can put the money paid to the children into a 529 plan or similar type of plan, for education. Note that in most cases, a 529 allows for a tax-free withdrawal for certain private school tuition for K-12.
  - Deductions for corporate vehicle
  - Maximizing retirement plans

Retirement Plans

- Retirement plans in general…
  - Defined Benefit Plans vs. Defined Contribution Plans
    - ◊ A Defined Benefit Plan (DBP) allows for a larger contribution than traditional 401k Plans.
      - The exact tax deductible contribution is derived by an actuary. The calculation is based on the amount needed to retire, age of participant, and cannot be more than $250,000.
      - If the contribution cannot be made by the company, then there is a 10% excise tax that the company has to pay
    - ◊ A Defined Contribution Plan
      - 401k Plans, SIMPLE, SEP, etc.

Potential Tax Savings Example

Bob 48 and is a surgeon. He is a Solo-Practioner. He is married, has two children, Mark and Samatha, aged 15 and 21, respectively. Both children live at home. His gross income from business is $1 million. After his expenses are paid, his taxable income is $500,000. His company is an S-Corporation, and his compensation is $200,000. His S-Corporation has not distributed $400,000, to him from prior years.

As a doctor (not to mention AGI limitations) the Section 199A deduction on QBI is not allowed on the profit from his S-Corporation. As a consequence, Bob is in the 37% tax bracket. Bob converts his S-Corporation to a C-Corporation in 2019

Potential Tax Savings (Con’t)

In 2019, Bob’s company generates $1.5 million in gross revenue. The expenses are as followed:

Salary		$250,000
Contribution to DBP	$180,000	
Salary to Mark		$6,000
Salary to Samatha	$6,000	
Payment to Samantha’s College		$5,100
Contribution to HRA	$10,000	
Health Insurance	$18,000	
Other Fringe Benefits	$10,000	
Other Expenses		<u>$200,000</u>
Taxable Income :		<u>$834,000</u>
Tax:		$175,329

Potential Tax Savings (Con't)

As an S-Corporation, Bob would not be able to deduct his health insurance, HRA contribution, and other fringe benefits. Further, his salary was $250,000, and his net taxable profit would be $872,000 ($834,000 adding back the health insurance, HRA contribution, and other fringe benefits). In 2019, he is precluded from the the Section 199A deduction on QBI. His personal taxable income would be $1,122,000 ($250,000 + $872,000). Generating a tax of approximately $406,260.

What Has Been Accomplished?

Outside of saving ~$350,000 in taxes, Bob has taken $235,100 for his use, tax-free. This includes his retirement plan, monies paid to his children, tuition, and fringe benefits.

Which Kinds of Companies Benefit the Most?

C-Corporations are not for every business. The situations where C-Corporations work best are:

1. High income earners (whereby the Section 199A deduction is not allowed on QBI, or begins to phase out)
2. Certain companies that would ordinarily be subject to AMT (AMT was eliminated for C-Corporations)
3. Companies that are eligible for the R&D Credit and R&D deductions
4. Companies that will have NOL carryforwards

Other C Corporation Planning Opportunties

C Corporation Advantages

- Medical plan
- On-premises meals and lodging
- Fiscal year
- Operations only (no real estate)
- 21% rate (but for how long)
- Concerns regarding double taxation

Other Disadvantages of C Corporation

- Additional tax return v. sole proprietorship
- Payroll taxes for owners
- Difficulty of switching to pass-through
  - To S corp. = BIG tax (especially cash basis issues)
  - To LLC/partnership = liquidation tax
- Risk of accumulated earnings tax

Long-Term Care Insurance

- Age-based deduction limits for individuals
- Deduction limits n/a to C corporation

Corporate-Provided Meals and Lodging

- Tax-free fringe benefit (Sec. 119)
- Owner benefit tax-free only if C corporation
- IRS examination attacks
- Ordinary and necessary expense for corporation (Sec. 162)
- Sec. 119 requirements
  - Meals (not groceries)
  - Condition of employment and convenience of employer
  - On business premises

Lodging

- Business premises
- Includes utilities, furnishings, supplies consumed in home

Meals

- Provided on non-working days qualify
- Employee spouse and dependents also qualify
- Outside of working hours, need noncompensatory business reasons
  - On-call for emergencies
  - No eating facilities within vicinity
  - Meals w/o lodging during business hours okay
- Discrimination allowed

Must be Meals

- Prepared by employer
  - Have corporate employee prepare groceries into meals
  - Employment agreement
  - Use corporate credit card to pay for groceries

Documentation

- Initial authorization with business reasons
- Employment contract requiring on-premises residency
- Employment duties: Meal preparation
- Residence <u>specifically</u> available by direct ownership or by lease
- Caution: Eventual taxable gain if residence sold
- Document need for presence
- Deductions denied if personally-owned residence rented to employer

Meals at 50%

- No 100% argument under Sec. 132 due to TCJA
  - Employee recreational, social functions remain 100% deductible
- All Sec. 119 meals nondeductible after 2025

Section 1202 Stock

Section 1202 – The 100% Exclusion

- A taxpayer, other than a corporation, may:
  - Exclude 100% of the gain on the sale of “Qualified Small Business Stock (QSBS)”
  - Acquired after September 27, 2010
  - Subject to certain limitations
  - Can be a sale or redemption by the corporation
    - ◊ As long as the redemption qualifies under Sec. 302
  - Liquidation qualifies as long as corporation has sold substantially all of its assets

Must be Acquired Directly from Issuing Corp.

- Can be owned by individual, trust, estate, partnership or S-Corporation
- Must acquire stock directly from issuing corporation
  - Can't be from another shareholder
  - Exception for gifts or death
- Can purchase stock for cash or other property
  - Exception – Qualifies if a Sec. 351 or Sec. 368 transaction
- Property is broadly defined as all tangible and intangible assets
- Founder stock should qualify
  - However, make sure to document and have some consideration or compensation for services under Sec. 83

Must be Acquired - Continued

- Can be issued in connection with partnership incorporation
- Can be issued upon exercise of warrants or options
  - As long it is directly with corporation
- Can be issued in exchange for convertible debt
  - Five year holding period starts with conversion
- If issued as part of compensation with restrictions
  - Five year holding period starts when final restriction lapses, or
  - When Sec. 83 election is made

Partnerships and S-Corporations

- Partnership can elect to be taxed as C corporation
- However, conversion must occur before FMV of assets (not equity) reaches $50 million
- Keeping partnership status during start-up stage to maximize loss flow-through is appropriate
- Conversion at profit-stage is most optimal
- S-Corporation can never qualify as QSBS
  - However, if converted to C corporation, subsequent purchases can qualify as QSBS
- Must be a C-corporation when stock is issued
- Built-in gain does not qualify for Sec. 1202 exclusion

Built-in Gain Exclusion Example

- Tom and Jerry have a 50/50 partnership with FMV of $10 million and adjusted tax basis of $1 million.
- They incorporate on January 1, 2019
- Tom sells his stock for $10 million on June 30, 2025
- $5 million of the gain is tax-free under Sec. 1202
- $4.5 million of the gain is subject to 23.8% capital gains tax (assuming highest rate)
- $500,000 is tax-free return of capital

Software

- Rights to computer software which produces royalties is treated as the active conduct of a trade or business

Industries

- Ineligible
  - Professional services
  - Athletics
  - Banking and financial services, brokerage
  - Farming, including raising or harvesting trees
  - Mineral extraction
  - Hospitality (hotel, restaurant or similar business)
- Eligible
  - Construction
  - Manufacturing
  - Wholesale
  - Retail

Aggregate Gross Assets Restriction

- Aggregate Gross Assets is the sum of cash and aggregate adjusted bases of all other property.
- If property is contributed to corporation, then FMV is used
  - Careful with incorporation of partnership since FMV is the requirement not adjusted tax basis
  - Includes goodwill
- $50 million applies at the time of the issuance of the stock
- If it exceeds $50 after issuance of the QSBS does not taint Sec. 1202

Surprise Disqualification

- $50 million limitation is based upon gross assets
- Corporation XYZ was formed from investors contributing $40 million of cash
  - Rather than contributing cash to corporation, the investors immediately purchased $60 million in assets encumbered with $20 million in debt and then contributed to the corporation
  - Since corporation exceeded $50 million gross asset limitation, the stock is NOT QSBS

QSBS Must Be Held at Least 5 Years

- Stock must be held at least 5 years to qualify
- If partnership incorporates, 5 year holding period starts at time of incorporation
  - Previous holding period by partnership is ignored
  - Even though Sec. 351 allows for tacking on of holding period, this is not applicable for Sec. 1202
- Holding period rule has certain exceptions for gifted stock or stock transferred in connection with shareholder’s death
- Certain hedges will toll holding period

Maximum Gain Deferral

- QSBS gain is limited to the **greater** of
  - $10 million
    - ◊ Reduced by cumulative gain recognized by taxpayer under Sec. 1202 in prior years applicable to same issuer of stock
  - 10 times the aggregate tax bases of the QSBS of that issuer disposed of during the year
- If QSBS gain exceeds the limits, then excess is taxed at 28%

Sec. 1202 Exclusions

- Gain exclusion is based on date stock issued:
  - 8/10/1993 through 2/17/2009 = 50%
  - 2/17/2009 through 9/27/2010 = 75%
  - 9/28/2010 and later = 100%
- If 100% exclusion applies:
  - No gain
  - No Net Investment Income Tax (NIIT)
  - Applies for regular tax and AMT

Exclusion Percentage – Regular and AMT tax

Acquistion Date	Exclusion Percentage	Maximum QSBS Rate	Maximum QSBS AMT Rate	Maximum Rate (No QSBS)
Aug. 11, 1993 to Feb. 17, 2009	50%	15.90%	16.88%	23.80%
Feb. 19, 2009 to Sep. 27, 2010	75%	7.95%	9.42%	23.80%
After Sep. 27, 2010	100%	0.00%	0.00%	23.80%

Gain Exclusion – 50% Example

- Gain exclusion limited to greater of:
  - 10 times adjusted basis in stock, or
  - $10 million

Example #1:

- Stock was issued 7/1/2008 for $900,000
- Sold in 2019 for $18 million
- Total gain is $17.1 million
- 50% exclusion applies = $8,550,000 potential exclusion
- Maximum exclusion, greater of
  - 10 x $900,000 = $9 million, or
  - $10 million
- Of the total gain of $17.1 million, $8,550,000 is taxable

75% Example

- Gain exclusion limited to greater of:
  - 10 times adjusted basis in stock, or
  - $10 million

Example #2:

- Stock was issued 7/1/2010 for $900,000
- Sold in 2019 for $18 million
- Total gain is $17.1 million
- 75% exclusion applies = $12,825,000 potential exclusion
- Maximum exclusion, greater of
  - 10 x $900,000 = $9 million, or
  - $10 million
- Of the total gain of $17.1 million, $7,100,000 is taxable

100% Example

- Gain exclusion limited to greater of:
  - 10 times adjusted basis in stock, or
  - $10 million

Example #3:

- Stock was issued 7/1/2011 for $900,000
- Sold in 2019 for $18 million
- Total gain is $17.1 million
- 100% exclusion applies = $17,100,000 potential exclusion
- Maximum exclusion, greater of
  - 10 x $900,000 = $9 million, or
  - $10 million
- Of the total gain of $17.1 million, $7,100,000 is taxable

100%, Different Amounts

- Gain exclusion limited to greater of:
  - 10 times adjusted basis in stock, or
  - $10 million

Example #3:

- Stock was issued 7/1/2011 for $900,000
- Sold in 2019 for $11 million
- Total gain is $10.1 million
- 100% exclusion applies = $10,100,000 potential exclusion
- Maximum exclusion, greater of
  - 10 x $900,000 = $9 million, or
  - $10 million
- Of the total gain of $10.1 million, $100,000 is taxable

Sec. 1202 Stock: Is 0% Efficient?

Advantages

- Operating income at lower C corp. rates
- Stock sale: (if fully excluded) no 3.8% NIIT and 0% 1040 capital gain tax

Disadvantages

- Limited industries eligible
- No use of operating losses; withdrawals taxable
- May be difficult to sell stock

Stock Redemptions

- Stock redemptions near stock issuance can eliminate QSBS
- Stock cannot qualify as QSBS if
  - Corporation has redeemed any stock from taxpayer or related parties during four-year period beginning two years before issuance of stock
    - ◊ Two years before and two years after
- Stock does not qualify if corporation has redeemed at least 5% of its stock within two year of issuance
- Redemptions due to termination of employment are ignored
- Redemptions due to death, disability or divorce are also ignored
- Redemptions can occur five years after issuance

Rollovers under Sec. 1045

- If taxpayer is forced or decides to sell before 5 year holding period
  - Can elect to roll over the stock under Sec. 1045
  - Within 60 days into other QSBS
  - Must have held stock for at least six months
  - New corporation must meet active business requirement for at least six months after rollover
  - Taxpayer must file election with IRS
  - Must meet all Sec. 1045 requirements

State Tax and Other Implications

- Sec. 1202 is a federal tax exclusion provision
- Many states will follow federal, however not all will
  - CA and PA completely disallow QSBS exclusion
  - Some states (e.g. MA, NJ, and HI) make modifications
- Sec. 1202 is not elective
- No reporting requirements
- 28% rate gain worksheet
- None of 100% gain exclusion is an AMT preference item
- Can you combine QSBS and Qualified Opportunity Zone to completely eliminate gain?
  - If you meet the 10 year holding period, etc.

S Corporation Versus C Corporation Examples

Low Tax Rate, Sec. 199A, State Taxes

Corporate federal tax rate	21.00%
Corporate state tax rate	7.00%
Individual federal tax rate	15.00%
Individual state tax rate	9.00%
Federal CG tax rate on liquidation	23.80%
Benefit of 199A	20.00%
Discount rate	5.00%
Assume no special state CG tax rate	

	C	S
Book income	$ 1,000,000	$ 1,000,000
Less state income tax	(70,000)	
Taxable income	$ 930,000	$ 1,000,000
Book income, before tax	$ 1,000,000	$ 1,000,000
Federal tax	(195,300)	
State tax	(70,000)	
Distributions in lieu of Federal tax		(120,000)
Distributions in lieu of state tax		(90,000)
Retained equity	734,700	790,000
# years accumulation	25	25
Liquidation value	18,367,500	19,750,000
Basis to shareholders	-	19,750,000
Capital gain, shareholders	18,367,500	-
Federal and state capital gains tax	32.80%	32.80%
Shareholder capital gain tax	$ 6,024,540	$ -
Present value of annual taxes	$ 3,739,123	$ 2,959,728
Present value of liquidation tax	1,779,063	-
	$ 5,518,187	$ 2,959,728

Low Tax Rate, Sec. 1202, State Tax, 199A

Corporate federal tax rate	21.00%
Corporate state tax rate	7.00%
Individual federal tax rate	15.00%
Individual state tax rate	9.00%
Federal CG tax rate on liquidation	0.00%
Benefit of 199A	20.00%
Discount rate	5.00%
Assume no special state CG tax rate	

	C	S
Book income	$ 1,000,000	$ 1,000,000
Less state income tax	(70,000)	
Taxable income	$ 930,000	$ 1,000,000
Book income, before tax	$ 1,000,000	$ 1,000,000
Federal tax	(195,300)	
State tax	(70,000)	
Distributions in lieu of Federal tax		(120,000)
Distributions in lieu of state tax		(90,000)
Retained equity	734,700	790,000
# years accumulation	25	25
Liquidation value	18,367,500	19,750,000
Basis to shareholders	-	19,750,000
Capital gain, shareholders	18,367,500	-
Federal and state capital gains tax	9.00%	9.00%
Shareholder capital gain tax	$ 1,653,075	$ -
Present value of annual taxes	$ 3,739,123	$ 2,959,728
Present value of liquidation tax	488,158	-
	$ 4,227,281	$ 2,959,728

Low Tax Rate, No 199A, Sec. 1202, State Tax

Corporate federal tax rate	21.00%
Corporate state tax rate	7.00%
Individual federal tax rate	15.00%
Individual state tax rate	9.00%
Federal CG tax rate on liquidation	0.00%
Benefit of 199A	0.00%
Discount rate	5.00%
Assume no special state CG tax rate	

	C	S
Book income	$ 1,000,000	$ 1,000,000
Less state income tax	(70,000)	
Taxable income	$ 930,000	$ 1,000,000
Book income, before tax	$ 1,000,000	$ 1,000,000
Federal tax	(195,300)	
State tax	(70,000)	
Distributions in lieu of Federal tax		(150,000)
Distributions in lieu of state tax		(90,000)
Retained equity	734,700	760,000
# years accumulation	25	25
Liquidation value	18,367,500	19,000,000
Basis to shareholders	-	19,000,000
Capital gain, shareholders	18,367,500	-
Federal and state capital gains tax	9.00%	9.00%
Shareholder capital gain tax	$ 1,653,075	$ -
Present value of annual taxes	$ 3,739,123	$ 3,382,547
Present value of liquidation tax	488,158	-
	$ 4,227,281	$ 3,382,547

Low Tax Rate, No 199A, Sec. 1202, No State

Corporate federal tax rate	21.00%
Corporate state tax rate	0.00%
Individual federal tax rate	15.00%
Individual state tax rate	0.00%
Federal CG tax rate on liquidation	0.00%
Benefit of 199A	0.00%
Discount rate	5.00%
Assume no special state CG tax rate	

	C	S
Book income	$ 1,000,000	$ 1,000,000
Less state income tax	-	
Taxable income	$ 1,000,000	$ 1,000,000
Book income, before tax	$ 1,000,000	$ 1,000,000
Federal tax	(210,000)	
State tax	-	
Distributions in lieu of Federal tax		(150,000)
Distributions in lieu of state tax		-
Retained equity	790,000	850,000
# years accumulation	25	25
Liquidation value	19,750,000	21,250,000
Basis to shareholders	-	21,250,000
Capital gain, shareholders	19,750,000	-
Federal and state capital gains tax	0.00%	0.00%
Shareholder capital gain tax	$ -	$ -
Present value of annual taxes	$ 2,959,728	$ 2,114,092
Present value of liquidation tax	-	-
	$ 2,959,728	$ 2,114,092

High Tax Rate, State Tax & Full 199A

Corporate federal tax rate	21.00%
Corporate state tax rate	7.00%
Individual federal tax rate	37.00%
Individual state tax rate	9.00%
Federal CG tax rate on liquidation	23.80%
Benefit of 199A	20.00%
Discount rate	5.00%
Assume no special state CG tax rate	

	C	S
Book income	$ 1,000,000	$ 1,000,000
Less state income tax	(70,000)	
Taxable income	$ 930,000	$ 1,000,000
Book income, before tax	$ 1,000,000	$ 1,000,000
Federal tax	(195,300)	
State tax	(70,000)	
Distributions in lieu of Federal tax		(296,000)
Distributions in lieu of state tax		(90,000)
Retained equity	734,700	614,000
# years accumulation	25	25
Liquidation value	18,367,500	15,350,000
Basis to shareholders	-	15,350,000
Capital gain, shareholders	18,367,500	-
Federal and state capital gains tax	32.80%	32.80%
Shareholder capital gain tax	$ 6,024,540	$ -
Present value of annual taxes	$ 3,739,123	$ 5,440,263
Present value of liquidation tax	1,779,063	-
	$ 5,518,187	$ 5,440,263

High Tax Rate, State Tax and No 199A

Corporate federal tax rate	21.00%
Corporate state tax rate	7.00%
Individual federal tax rate	37.00%
Individual state tax rate	9.00%
Federal CG tax rate on liquidation	23.80%
Benefit of 199A	0.00%
Discount rate	5.00%
Assume no special state CG tax rate	

	C	S
Book income	$ 1,000,000	$ 1,000,000
Less state income tax	(70,000)	
Taxable income	$ 930,000	$ 1,000,000
Book income, before tax	$ 1,000,000	$ 1,000,000
Federal tax	(195,300)	
State tax	(70,000)	
Distributions in lieu of Federal tax		(370,000)
Distributions in lieu of state tax		(90,000)
Retained equity	734,700	540,000
# years accumulation	25	25
Liquidation value	18,367,500	13,500,000
Basis to shareholders	-	13,500,000
Capital gain, shareholders	18,367,500	-
Federal and state capital gains tax	32.80%	32.80%
Shareholder capital gain tax	$ 6,024,540	$ -
Present value of annual taxes	$ 3,739,123	$ 6,483,215
Present value of liquidation tax	1,779,063	-
	$ 5,518,187	$ 6,483,215

High Tax Rate, State Income Tax, No 199A, Sec. 1202 at Federal Level Only

Corporate federal tax rate	21.00%
Corporate state tax rate	7.00%
Individual federal tax rate	37.00%
Individual state tax rate	9.00%
Federal CG tax rate on liquidation	0.00%
Benefit of 199A	0.00%
Discount rate	5.00%
Assume no special state CG tax rate	

	C	S
Book income	$ 1,000,000	$ 1,000,000
Less state income tax	(70,000)	
Taxable income	$ 930,000	$ 1,000,000
Book income, before tax	$ 1,000,000	$ 1,000,000
Federal tax	(195,300)	
State tax	(70,000)	
Distributions in lieu of Federal tax		(370,000)
Distributions in lieu of state tax		(90,000)
Retained equity	734,700	540,000
# years accumulation	25	25
Liquidation value	18,367,500	13,500,000
Basis to shareholders	-	13,500,000
Capital gain, shareholders	18,367,500	-
Federal and state capital gains tax	9.00%	9.00%
Shareholder capital gain tax	$ 1,653,075	$ -
Present value of annual taxes	$ 3,739,123	$ 6,483,215
Present value of liquidation tax	488,158	-
	$ 4,227,281	$ 6,483,215

High Tax Rate, No State Tax, No 199A, Sec. 1202

Corporate federal tax rate	21.00%
Corporate state tax rate	0.00%
Individual federal tax rate	37.00%
Individual state tax rate	0.00%
Federal CG tax rate on liquidation	0.00%
Benefit of 199A	0.00%
Discount rate	5.00%
Assume no special state CG tax rate	

	C	S
Book income	$ 1,000,000	$ 1,000,000
Less state income tax	-	
Taxable income	$ 1,000,000	$ 1,000,000
Book income, before tax	$ 1,000,000	$ 1,000,000
Federal tax	(210,000)	
State tax	-	
Distributions in lieu of Federal tax		(370,000)
Distributions in lieu of state tax		-
Retained equity	790,000	630,000
# years accumulation	25	25
Liquidation value	19,750,000	15,750,000
Basis to shareholders	-	15,750,000
Capital gain, shareholders	19,750,000	-
Federal and state capital gains tax	0.00%	0.00%
Shareholder capital gain tax	$ -	$ -
Present value of annual taxes	$ 2,959,728	$ 5,214,759
Present value of liquidation tax	-	-
	$ 2,959,728	$ 5,214,759

Questions

Craig Smalley, EA
craig@cwseapa.com
844-297-3272
Cwseapa.com

Paul Neiffer, CPA
Paul.Neiffer@claconnect.com
509-823-2920
Claconnect.com
Blog: www.farmcpatoday.com