2018 Tax Reform
Fiscal Year-ends

Presenters

Brandy Vannoy, CPA
Partner
Johnson Lambert LLP

Matt Gravelin, CPA
Principal
Johnson Lambert LLP

Agenda

- Current tax calculation
- Deferred calculation
- Footnote disclosures
- Future guidance that will be necessary

Current Tax Calculation

- Internal Revenue Code ("IRC") §15
  - Directs how to treat rate differences that become effective during a tax year
  - Applies when the effective date of a tax rate change is <u>not</u> the first day of the tax year
  - Requires pro-rata bifurcation based on the number of days in each period

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Current Tax Calculation

- Example – fiscal year-end of June 30, 2018
  - Taxable income of $8,000,000

$8M x 34% x 6 months / 12 months

$1,360,000

$8M x 21% x 6 months / 12 months

$840,000

Total tax
$2,200,000

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Current Tax Calculation

- Example – fiscal year-end of June 30, 2018
  - Taxable income of $8,000,000

Q1	Q2	Q3	Q4
$1M x 34%	$1M x 34%	$4M x 21%	$2M x 21%
$340,000	$340,000	$840,000	$420,000

Total tax
$1,940,000

Current Tax Calculation

- Example – fiscal year-end of December 25, 2017
  - Taxable income of $8,000,000
  - $8,000,000 x 34% = $2,720,000
  - No change from current calculation

Deferred Taxes

- Fiscal year ending on December 25, 2017
  - The Act was enacted during the tax year (i.e. December 22nd)
  - Apply the enacted rate expected for the tax year those deferred items would be realized
  - Deferred inventory valued at 21%

Tax Footnote Disclosures

- Fiscal year-end after December 22, 2017

Current

Current federal income taxes incurred by the Company are determined by applying statutory tax rates to taxable income as determined according to the provisions of the Internal Revenue Code, which apply to property and casualty insurance companies. The Tax Cuts and Jobs Act of 2017 (the "Act") reduced the tax rate effective January 1, 2018 to a flat 21%. The Company's blended tax rate was **XX%** for the fiscal year ended June 30, 2018 and 34% for the year ended June 30, 2017.

Deferred

On December 22, 2017, the Tax Cuts and Jobs Act (the "Act") was signed into law. We have recorded a tax **benefit/expense** of **$XX**, primarily due to the re-measurement of deferred tax assets and liabilities from **XX** percent to a flat 21 percent. The Company is currently in the process of determining the full effects of the Act on our business and financial results, but believes all material items impacting the Company as a result of the Act are reflected within these financial statements.

Deferred Taxes

- Fiscal year ending on November 30, 2017
  - Must apply tax rates that are enacted for the reporting period
  - Value deferred at 34% or the estimated effective rates that would apply under the graduated structure

Subsequent Event Disclosure

- Fiscal year-end before December 22, 2017 – for financial statements not issued yet

On December 22, 2017, the Tax Cuts and Jobs Act (the "Act") was signed into law. We are in the process of analyzing the Act and its possible effects on the Company. The Act reduces the corporate tax rate from **XX** percent to a flat 21 percent, among other things. It will also require us to write down our deferred tax **assets/liabilities**, which would **reduce/increase** our net income and shareholder's equity during the fiscal year ending in 2018. The Company is currently in the process of determining the full effects of the Act on our business and financial results.

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Final Thoughts

- IRC §15 only addresses rate differences – what about items such as:
  - Dividends received deduction
  - Meals and entertainment
  - Net operating losses
  - Loss discounting
  - Others???

Final Thoughts

- Do you need to apply a similar blended rate based on number of days?

- Or, do you need to use actual amounts received or paid during the respective periods?

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Final Thoughts

- Dividend received deduction
  - Effective for tax years <u>beginning after</u> 2017
- Meals and entertainment
  - Effective for <u>amount paid or incurred after</u> December 31, 2017

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Final Thoughts

- Net operating losses
  - Carryforward limitation of 80% - effective for losses arising in tax year <u>beginning after</u> 2017
  - Indefinite carryforward an elimination of the carryback period – effective for losses arising in tax year <u>ending after</u> 2017

- We will need technical guidance and/or further clarifications from IRS

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