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How 40 Ambiguities (and Outright Errors) in the New Tax Law Could Cost You Big Money

Ambiguities in the nearly 600-page document could have costly consequences for entrepreneurs, experts say.

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Many entrepreneurs have celebrated President Trump's signature legislative achievement, the 2017 Tax Cuts and Jobs Act, for decreasing their annual tax bills. Indeed, the law reduces the maximum corporate tax rate from 35 percent to 21 percent, and further allows pass-through firms to deduct up to 20 percent of their business income, excepting personal services. But a series of errors and ambiguities in the language of the law could mean losses for hundreds of businesses, keeping tax preparers busy this season.

"For many retailers, there's going to be a cash flow hit," suggests Rachelle Bernstein, vice president and tax counsel at the Washington, D.C.-based National Retail Federation, a trade association, who notes that many of her clients are already shoring up costs in preparation for a higher tax bill in 2018. "Some companies have told me that they were planning on passing on their tax savings to workers and boost wages, but can no longer do so until this is resolved," she adds.

In particular, Bernstein is referring to Sec. 13204/168 (3), an element of the law that intended to simplify depreciation rules for businesses making renovations or other property improvements, such that these expenses could be deducted from the company's tax billover 15 years. Because of a clerical error, however, these costs must be deducted over 39 years, diminishing the bonus that dozens of restaurants and retailers had expected to receive, and for which many have already begun spending. "Say I invested $100,000 in property renovations in 2018," explains Bernstein. According to the intended depreciation rules, "I should be able to get the full $100,000 back [after filing my taxes.] Instead, the way the law is written, I will only get a 2.5 percent write off, or $2,500," she adds.

The lack of clarity around real property investments is just one of more than 40 issues that the U.S. Chamber of Commerce recently highlighted in a letter sent to the Department of Treasury last Thursday. The 15-page document requests clarification on how the law affects multinational corporations and pass-through firms across the country. "The Chamber strongly urges the Treasury and the I.R.S. to work closely with the business community to implement the recent tax changes in a manner to ensure as little disruption as possible to normal business operations and to ensure this law encourages the U.S.

economy to achieve its growth potential," noted Caroline Harris, vice president of tax policy at the Chamber, in the letter.

Another pressing error impacting independent agriculture firms, in particular, is what analysts are referring to as the "grain glitch." It's an eleventh-hour addition to the tax law, permitting farmers to deduct 20 percent of their total sales to cooperatives, which are agricultural organizations owned by groups of farmers. Dozens of local processors, however, insist that the loophole is reducing their competitiveness, inasmuch as farmers are now more likely to sell to the coops to get the write off.

David Gamage, a professor of tax law and policy with Indiana University's Maurer School of Law, notes that many companies are now looking to restructure themselves as coops torecoup the lost sales. Still, "there are costs to everyone considering restructuring," he says. "If you think that Congress is going to fix this soon, maybe you wait and see, but I wouldn't wait too long, and potentially lose quite a bit of business to competitors," he advises.

Of course, all of this could be assuaged if the Treasury and the I.R.S. simply issue a technical correction to the grain glitch and depreciation rules, respectively, though it's unclear when that could come. It's also worth pointing out that technical errors, such as the above, are not unheard of. The NRF's Bernstein says she counts some 7 technical correction bills that have been issued over the past 25 years. Others, however, say the gravity of these issues is far more substantial than ever before. "Stuff like this happening isn't unique, but the order of magnitude is completely unprecedented," says Indiana's Gamage.

Drawing the Line

To his point, while cooperative and property deductions are likely to be handled in an efficient manner, there are other, more ambiguous issues with the current tax law. In particular, analysts point to a provision that allows pass-through entities to deduct up to 20 percent of their Qualified Business Income, although it is unclear to whom exactly this deduction might apply, since certain 'professional services' are exempt. "There is a vague sense that the drafters want to offer the deduction to businesses that aren't service types, but exactly how you draw the line is very hard to figure out from reading the statute," suggests Gamage.

Indeed, the lack of clarity vis-à-vis pass throughs has led many partnerships to consider restructuring altogether as C-corporations, to avoid the whole depreciation aspect--and to access the reduced maximum tax rate of 21 percent. Edward Reitmeyer, a partner with the New York City global accounting firm Marcum LLP, notes that several of his clients are seriously considering the move. "It's really being discussed, but you'll see that for the most part, everyone is couching that advice," he adds, referring to the possibility that the law could be tweaked to bring greater clarity for business owners. Other analysts caution against restructuring, inasmuch as pass-through firms could potentially be taxed twice--once on the 21 percent preferential rate, and again if and when the owners pay dividends. "The two levels of tax would make a corporate operation less advantageous than a partnership," suggested William Kambas, a partner with the international law firm Withers Worldwide, in an earlier phone call with Inc.

Ultimately, many entrepreneurs are wise to get creative this season, or risk losing out on valuable savings. "Unfortunately, almost any business with substantial income that doesn't want to leave easy money on the table probably needs to spend," suggests Gamage. "Any business currently structured as a pass-through needs to get good legal or accounting advice to even start to work through their basic options."