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Conversation Starter

Tax reform and your business structure:
Should your pass-through business convert to a C corporation?

The lowered corporate tax rate under the *Tax Cuts and Jobs Act* of 2017 means some pass-through entities could lessen their tax burdens by converting to C corporations. However, there are some key considerations – including other provisions of the tax reform bill – to keep in mind before changing your business structure.

Pass-throughs v. C-corps: relevant changes from the TCJA

	Pass-through business (S corporation, partnership, LLC)	C corporation
Tax rate	Top bracket for individual owners now 37% (down from 39.6%)	Corporate rate reduced from a top rate of 35% to a flat 21%
Qualified business income (QBI) deduction	Up to 20% of QBI now deductible (many service businesses excluded)	Not applicable
State tax deduction	State tax deduction for individual owners now limited to $10,000	No limit on state tax deduction
Tax on foreign income	Full inclusion of global intangible low-taxed income (GILTI); 37% effective rate on qualified foreign income in top bracket Not affected by foreign-derived intangible income (FDII) or base erosion anti-abuse tax (BEAT) provision	50% inclusion of GILTI income (10.5% effective rate on qualified foreign income through 2025) FDII deduction applies; BEAT applies if gross receipts total $500 million or more
Income from foreign operations or partnerships	Taxable in U.S.; most income will be ineligible for 20% pass-through entity deduction	Taxable in U.S.
Income from foreign subsidiaries earned after Jan. 1, 2018	Generally not taxed when earned, but taxed in U.S. when received as dividend	Generally exempt from U.S. taxation when earned or distributed

Pass-throughs v. C-corps: existing tax provisions to consider

	Pass-through business (S corporation, partnership, LLC)	C corporation
3.8% tax on net investment income for high-income individuals	Applies to owners who are not active in the business, including gain on sale	Applies to dividends and gains from the sale of stock even if the owner is active in the business
Self-employment tax	Principally applies to active owners of partnerships and LLCs	Not applicable
Tax basis in investment	Income increases owner basis; losses and distributions decrease owner basis	In most cases, calculated from cost basis
Distributions	Generally tax free up to basis; capital gains tax applies to distributions in excess of basis	Generally taxed as dividends
Proceeds from sale of business	Mostly taxed as capital gains, though some income could be taxed as ordinary income	Taxed as capital gains

Before deciding on any changes to your business structure, talk to the trusted tax professionals at Crowe. One of the top 10 U.S. accounting and consulting firms, we have the deep industry knowledge and decades of experience to help you make more informed decisions and add value to your organization. **Learn more: crowe.com/services/tax**