

On December 19, 2017, the House and Senate passed the conference report of the Tax Cuts and Jobs Act (H.R. 1). ICBA has been deeply engaged in the tax reform process since it began in earnest some 18 months ago. We are grateful to the thousands of community bankers who have joined in our grassroots efforts. [Click here](#) for a copy of the letter we sent to the Conference Committee on H.R. 1.

The scorecard below describes outcomes on provisions of direct importance to community banks.

FAVORABLE OUTCOMES

CORPORATE RATE

The conference agreement establishes a corporate rate of 21 percent (down from 35 percent) effective January 1, 2018. This provision is permanent.

ICBA Advocacy

ICBA advocated for the lowest possible tax rate for C corporation community banks with the quickest possible effective date. The Senate-passed version of H.R. 1 had an effective date of January 1, 2019. Moving the effective date forward will help banks mitigate any lost value of deferred tax assets. A lower corporate rate will reduce the competitive advantage of credit unions and Farm Credit System lenders.

SUBCHAPTER S / PASS-THROUGH RATE

The conference agreement allows shareholders of Subchapter S community banks to deduct 20 percent of their business income, which will be taxed at the new reduced ordinary individual rates. This deduction is available to shares held in trusts and estates. The bill will also limit this deduction to 50 percent of W-2 compensation paid by the business. The limitation will not affect joint filers with taxable income of less than \$315,000 or individual filers with taxable income of less than \$157,500. The 20 percent deduction will sunset at year-end 2025.

ICBA Advocacy

ICBA led the grassroots effort to create greater parity between S and C corporation community banks and to ensure the 20% deduction was available to trusts and estates. Though the final agreement falls short of parity, it was dramatically improved during the legislative process.

ICBA's grassroots campaign on this issue has generated thousands of contacts to key lawmakers.

BUSINESS INTEREST DEDUCTION

In the conference agreement, businesses with gross annual receipts of \$25 million or less will continue to deduct their interest expense in full. Businesses above this threshold will be limited to deducting net interest expense of no more than

30 percent of “adjusted taxable income” or earnings before interest, taxes, depreciation, and amortization (EBITDA). Beginning in 2022, EBIDA will be replaced by earnings before interest and taxes (EBIT).

Banks will not be directly affected because the limitation applies only to net interest expense.

The conference agreement also provides that any real property development, redevelopment, construction, reconstruction, acquisition, conversion, rental, operation, management, leasing, or brokerage trade or business is exempt from any limitation on interest deduction. In addition, a “farming business” may elect not to be subject to the above limitation on deducting interest.

The conference agreement is more favorable than the Senate version of H.R. 1, which fully exempted businesses with \$15 million or less in gross annual receipts or with net interest expense of less than 30 percent of EBI.

ICBA Advocacy

For the past 20 months, ICBA has campaigned to protect the business interest deduction. It was the primary focus of our August tax reform white paper and direct lobbying. ICBA’s grassroots campaign on this issue has generated thousands of contacts to key lawmakers as well as an op-ed campaign in selected markets.

NON-QUALIFIED DEFERRED COMPENSATION

Non-qualified deferred compensation (NQDC) plans are widely used by community banks to supplement the pension income of key employees. The House and Senate bills originally included a provision that would have effectively ended deferred compensation (which is often funded by Bank-Owned-Life-Insurance (BOLI)) by taxing it as soon as it is vested. This provision was removed from both bills.

ICBA Advocacy

ICBA advocated for the preservation of NQDC.

MORTGAGE PROVISIONS

The House version of H.R. 1 would have limited the mortgage interest deduction to interest paid on the first \$500,000 of acquisition debt on a principle residence. The House version would have repealed the deduction for second home and HELOC interest. The Senate version of H.R. 1 would have repealed the deduction for HELOC interest. The conference agreement limits the mortgage interest deduction to interest paid on the first \$750,000 of acquisition debt on a first or a second home. (The \$750,000 is a combined limitation.) The conference agreement also suspends the deduction for HELOC interest until 2026.

The House and Senate versions of H.R. 1 would have increased the length of time a taxpayer must own and live in a home in order to qualify for the capital gains exclusion from two out of the last five years to five out of the last eight

years. The House version would have also phased out the exclusion for higher income taxpayers. The conference agreement preserves current law.

ICBA Advocacy

ICBA worked with a coalition of mortgage lenders and other interested groups to improve the provisions described above.

The Senate Finance Committee version of H.R. 1 would have required upfront taxation of mortgage servicing fee income. This provision was removed prior to consideration on the Senate floor and is not in the conference agreement.

ICBA Advocacy

ICBA's grassroots campaign on this issue has generated hundreds of targeted contacts to key lawmakers.

ESTATE TAX

The conference agreement doubles the estate tax exemption but does not repeal the tax. The higher exemption level is indexed to inflation but will expire at year-end 2025.

ICBA Advocacy

ICBA advocated for full repeal of the estate tax.

CORPORATE ALTERNATIVE MINIMUM TAX

The Senate-passed version of H.R. 1 included the corporate alternative minimum tax. Because the corporate rate, at 20 percent, would have been equal to the AMT rate, the corporate AMT could have effectively nullified the tax exemption for municipal bond interest, among other exemptions and credits. The conference agreement fully repeals the corporate AMT.

ICBA Advocacy

ICBA advocated for full repeal of the corporate AMT.

INTEREST ON PRIVATE ACTIVITY AND MUNICIPAL BONDS

The House bill repealed the tax exemption for newly issued private activity bonds. The conference agreement preserves this tax exemption.

ICBA Advocacy

ICBA advocated for preservation of the tax exemption on these bonds.

NEW MARKETS TAX CREDIT

The House bill would have terminated the new markets tax credit (NMTC). NMTC is a critical tool for ensuring that economic growth reaches low-income urban and rural communities. It was preserved in the conference report.

ICBA Advocacy

ICBA is urged Congress to restore this important tax credit.

ONGOING CHALLENGES

DEFERRED TAX ASSETS

ICBA is fully aware that the sharp reduction in the corporate tax rate will cause a one-time devaluation of deferred tax assets (DTAs) with implications for both earnings and regulatory capital. The use of DTAs is limited in capital calculations. As noted above, ICBA believes the 1/1/2018 effective date of the new corporate tax rate will mitigate the impact of DTA devaluation. (In the Senate bill, the new rate would have been effective 1/1/2019). ICBA is in contact with the regulatory agencies and is urging them to issue guidance to address the potential impact of DTA devaluation.

CREDIT UNION AND FARM CREDIT SYSTEM TAX SUBSIDIES

ICBA is disappointed that the conference agreement fails to eliminate or curtail the generous taxpayer subsidies given to credit unions and Farm Credit System (FCS) lenders. The conference report to H.R. 1 notes that: "While significant differences between the rules under which credit unions and banks operate have existed in the past, most of those differences have disappeared over time." This language plainly acknowledges that the tax-exemption has outlived its original justification. This is the unfinished business of tax reform. ICBA will continue to advocate for repeal or modification of these egregious tax subsidies.

TAX DEDUCTION FOR FDIC PREMIUMS

The conference agreement phases out this deduction for banks between \$10 billion and \$50 billion. No deduction will be available for banks over \$50 billion. ICBA strongly objected to this provision. FDIC premiums are clearly a business expense as is any other form of insurance premium.

INTEREST ON HOME EQUITY LINES OF CREDIT

The conference agreement repeals the deduction for interest paid on HELOCs from 2018 to 2026. Interest on HELOCs used for expansion of improvement of a primary residence continues to be tax deductible.

INDIVIDUAL ALTERNATIVE MINIMUM TAX

The conference agreement raises the AMT exemption amount from \$84,500 to \$109,400 for joint filers and the exemption phase-out threshold from \$160,900 to \$1 million for joint filers. ICBA advocated for full repeal of the individual AMT.

NET OPERATING LOSSES

The conference agreement prohibits carryback of net operating losses. Losses that are carried forward are limited to 80 percent of taxable income.

TAXATION OF CREDIT CARD FEE INCOME

The conference agreement requires upfront taxation of credit card fee income. This change will increase rates and fees paid by consumers and potentially dampen consumer spending.

Please contact Alan Keller (alan.keller@icba.org) or John Hand (john.hand@icba.org) if you have any questions about H.R. 1.