

Is it Possible to Do More With Less When it Comes to Race Horses?



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Premise:

Tax policy does matter to horse racing and
breeding

Affect of the Tax Reform Act of 1986 on Horse Racing and Breeding

- Lower marginal rates and new active/passive activity distinctions led to major **owner shortage**
- Dramatic decline in **foal crop (-25% in six years; -60% today)**
- **Thoroughbred yearling prices** were crushed (-35%)
- Precipitous drop in the **number of starters per year (-22%)**
- **Handle flattened** after years of steady increases

Question:

If enacted, will the 2017 Tax Reform package help or hurt the Thoroughbred industry?

2017 TAX REFORM AND ITS IMPACTS ON THE THOROUGHBRED INDUSTRY

Following are the key provisions of the 2017 Tax Reform Package

This is a very fluid process changing hourly

Key issues and differences between the House and Senate versions:

ISSUE	HOUSE BILL	SENATE BILL
Individual Rates	4 brackets ranging from 12% -39.6%	7 brackets ranging from 10%-38.5%
State/Local Tax Deduction	Repeal SALT deductions for income + sales tax	Full repeal of all SALT deductions
Corporate Tax Rate	20%	20%
Estate Tax	Immediately doubles basic exclusion; full repeal after 2024	Immediately doubles basic exclusion; no full repeal
Obamacare Taxes	No change	Repeals individual mandate

Positive Provisions

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- **Increased Section 179 Expensing limits**, which would be beneficial to industry participants that generate net taxable income.

Areas of Concern

- **Like-kind exchanges** of horses, equipment and vehicles would be eliminated.

Areas of Concern

- **Limitation on the deductibility of business interest expenses.**
 - Limits net interest expense deduction to **no more than 30%** of adjusted taxable income
 - Exempts businesses with average annual gross receipts under **\$25 million (House)**; under **\$15 million (Senate)**
 - Senate allows a farming business to elect **not** to be subject to this limitation but then must depreciate any farm property with a **recovery period of 10 years or more**

Areas of Concern

- **Treatment of pass-through entities**
 - Applies to sole proprietorships, partnerships, LLCs, and S corps
 - **25% max rate** on pass through income (House); **17.4% deduction** on pass through income (Senate)
 - House and Senate versions differ in other **very technical ways**
 - Changes could have a **positive, negative, or neutral** effect on racing and breeding ops, depending upon the **individual circumstances**
 - However, this provision could **benefit majority of industry entities**

Areas of Concern

- **Net operating loss (NOL) carryback period**
 - Currently **5 years** for a farming loss, a **2-year** carryback for other business losses and a **20-year** carryforward period for those losses.
 - House and Senate bills would basically **eliminate carryback period** and **limit amount one can carryforward**

Areas of Concern

- **Limit on Wagering losses**
 - Both House and Senate bills **limit wagering losses** including all gambling-related deductions to the extent of winnings
 - This provision preserves recent regulatory change to withholding and reporting, which has led to a **95 percent decrease** in the number of W-2G filings
 - Negatively impacts **professional gamblers** who can currently deduct additional losses over and above losing wagers.

Areas of Concern

- **Entertainment Expenses**

- Both House and Senate bills disallow deductions for **entertainment** activities (50% deductible to 0% deductible)
- Could negatively impact racetracks and other operations whose patrons current deduction the cost of seating and other entertainment expenses
- This disallowance includes food and beverage expenses (House bill)

Areas of Concern

- **Charitable Contributions**

- Neither the House or Senate bills disallow charitable deductions but changes may discourage giving to **racing-related charities**
 - Doubling of the **standard deduction** to \$24K for joint filers will mean the vast majority of tax payers no longer itemize - \$13 Billion impact
 - **Repeal/reduction of gift and estate taxes** – currently they are a major incentive for giving

Areas of Concern

- **Capital Gains Holding Period**

- The industry has long sought a change in the **capital gains holding period** for horses from two years to one.
- While we continue to advocate for this, it is uncertain whether it will appear in the final tax package.

Areas of Concern

- **3-year Depreciation for Race Horses**
 - Industry has long sought level **3-year depreciation** for race horses
 - Currently, horses put into service as 2-year olds must be depreciated over 7 years
 - 100% bonus depreciation is available but will be phased out by 2024

Timetable

- House has passed its tax reform bill
- Senate has passed its tax reform bill
- A committee has been formed to reconcile differences between the two bills
- Final product would then be considered by both bodies.
- Passage in both chamber would send the bill to the President for signature.

Conclusion

Premise: Tax policy does matter to horse racing and breeding

Question: Is the 2017 Tax Reform package help or hurt the Thoroughbred industry?

Answer: On Balance, it could be a good thing but the “devil is in the details”