Tax Cuts and Jobs Act 2017

Tax Cuts and Jobs Act of 2017

Posted September 17, 2018

Welcome to your Tax Cuts and Jobs Act of 2017 and tax reform summary. A lot of this applies to 2018 tax returns which are due in 2019.

Read on for your dose of “oh what do we have to look forward to now?” If you have any questions you can always contact us for perplexed looks and the occasional clarification.

2018 Tax Brackets

Here is a comparison-

Single

Current Law		**Tax Cuts and Jobs Act**	
10%	$0 – $9,525	10%	$0 – $9,525
15%	$9,526 – $38,700	12%	$9,526 – $38,700
25%	$38,701 – $93,700	22%	$38,701 – $82,500
28%	$93,701 – $195,450	24%	$82,501 – $157,500
33%	$195,451 – $424,950	32%	$157,501 – $200,000
35%	$424,951 – $426,700	35%	$200,001 – $500,000
39.6%	$426,701+	37%	$500,000+

Married Filing Jointly

Current Law		**Tax Cuts and Jobs Act**	
10%	$0 – $19,050	10%	$0 – $19,050
15%	$19,051 – $77,400	12%	$19,051 – $77,400
25%	$77,400 – $156,150	22%	$77,400 – $165,000
28%	$156,151 – $237,950	24%	$165,01 – $315,000
33%	$237,951 – $424,950	32%	$315,01 – $400,000
35%	$424,951 – $480,050	35%	$400,001 – $600,000
39.6%	$480,050+	37%	$600,000+

Standard Deduction

Standard deduction to $12,000 on single returns, $18,000 for head-of-household filers and $24,000 on joint return.

Personal Exemptions

Gone. Zip. Zero. See ya. Lawmakers are scrambling to determine how to translate W-4 exemptions based on 2017 data for 2018 where exemptions are now removed from the calculus. Payroll departments are losing their minds. Not like they were that friendly to begin with.

Child Tax Credit

Starting in 2018, the $1,000 tax credit for each child under age 17 is doubled to $2,000, with $1,400 of the credit refundable to lower income taxpayers. Additionally, the package significantly increases the income phase-out thresholds. The credit begins to phase out for couples with adjusted gross incomes over $400,000 (up from $110,000 in 2017) and $200,000 for all other filers (up from $75,000).

Having kids is still really really really expensive. Don't be fooled! We heard that great danes are a much better choice.

Mortgage Interest

Lawmakers decided to reduce – from $1,000,000 to $750,000 – the amount of debt on which homeowners can deduct mortgage interest. The limit applies to mortgage debt incurred after December 15, 2017, to buy or improve a principal residence or second home. Older loans are still subject to the $1 million cap.

The law also bans the deduction of interest on home-equity loans. And this change applies to both old and new home-equity debt. Interest accrued on home-equity debt after December 31, 2017, is not deductible. So buying that boat with house money is still a good idea… just not deductible.

A proposal to extend the time you must own and occupy a home to qualify for tax-free profit when you sell it was dropped from the final legislation. As in the past, the law allows you to shelter up to $250,000 of such profit, or $500,000 if you're married, as long as you have owned and lived in the house for two of the five years before the sale.

Technically it is 24 out of 60 months, and you must wait two entire tax return cycles before using the exemption again.

Property Taxes et al

The deduction for what you pay in state and local income, sales and property taxes is also getting squeezed. This is commonly referred to as SALT deductions (State And Local Tax). People commonly say SALT deductions and property taxes. Property taxes are inclusive of state and local tax… it is like saying drugs and alcohol. Alcohol is a drug. SALT deductions include all taxes imposed by your state or local jurisdiction.

Starting in 2018, the new law sets a $10,000 limit on how much you can deduct of the state and local taxes you pay. A plan to limit the write-off to property taxes only was scrapped. You can deduct any combination of state and local income or sales taxes or residential property taxes, up to the $10,000 cap.

Additionally, under the new rules, property and sales taxes will remain deductible for taxpayers in a business or for-profit activity. For example, if you own a residential rental property, you can continue to fully deduct property taxes paid on that property on Schedule E. In other words, no change.

Unreimbursed Employed Expenses (Form 2106)

Gone. Pilots, flight attendants, truck drivers and railroad engineers used to get a massive deduction for per diem and travel expenses. Not anymore, unfortunately. Basically, the new law also repeals all miscellaneous itemized deductions subject to the 2% of AGI threshold, including the write-off for tax preparation fees, unreimbursed employee business expenses and investment fees.

Medical Expenses

Despite efforts to eliminate the deduction for medical expenses, the new law is actually more generous than the old one. Under the old rules, medical expenses were deductible only to the extent they exceeded 10% of adjusted gross income. For 2017 and 2018, however, the threshold drops to 7.5% of AGI. Come 2019, the 10% threshold returns.

This seems to coincide with the ACA penalty abatement slated for 2019.

Alimony

A big change is coming for divorce. In the past, alimony paid under a divorce decree was deductible by the ex-spouse who paid it and treated as taxable income by the recipient. Starting with alimony paid under divorce or separation agreements executed after December 31, 2018, the reverse will be true: Payors will no longer get to deduct alimony, but the payments will be tax-free for the ex-spouse who receives them. (That's the same rule that has and will continue to apply to child support payments.)

Roth Conversions

The new law will make it riskier to convert a traditional individual retirement account to a Roth. Under the old law, you could reverse such a conversion — and eliminate the tax bill — by "recharacterizing" the conversion by October 15 of the following year. Starting in 2018, such do-overs are done for. Conversions will be irreversible.

Stock Sales

For a while, it looked like Congress might restrict the flexibility investors have to control the tax bill on their profits. Investors who have purchased stock and mutual fund shares at different times and different prices are allowed to choose which shares to sell in order to produce the most favorable tax consequences. You can, for example, direct your broker to sell shares with a high tax basis (basically, what you paid for them) to limit the amount of profit you must report to the IRS or, if the shares have fallen in value, to maximize losses to offset other taxable gains. (Your gain or loss is the difference between your basis and the proceeds of the sale.)

The Senate called for eliminating the option to specifically identify which shares to sell and instead impose a first-in-first-out (FIFO) rule. The oldest shares would be assumed to be the first sold. Because it is assumed that the older shares likely have a lower tax basis, this change would trigger the realization of more profit sooner rather than later.

In the end, though, this idea fell by the wayside. Investors can continue to specifically identify which shares to sell to arrange for the most favorable tax outcome.

Capital Gains

The new law retains the favorable tax treatment granted long-term capital gains and qualified dividends, imposing rates of 0%, 15%, 20% or 23.8%, depending on your total income.

In the past, your capital gains rate depended on what tax bracket you fell in. But, with the changes in the brackets, Congress decided to set income thresholds instead. For example, the 0% rate for long-term gains and qualified dividends will apply for taxpayers with taxable income under about $38,600 on individual returns and about $77,200 on joint returns.

Section 199A Qualified Business Income Deduction

The new law slashes the tax rate on regular corporations (sometimes referred to as "C corporations") from 35% to 21%, starting in 2018. The law offers a different kind of relief to individuals who own pass-through entities — such as S corporations, partnerships and LLCs — which pass their income to their owners for tax purposes, as well as sole proprietors who report income on Schedule C of their tax returns. Starting in 2018, many of these taxpayers will be allowed to deduct 20% of their qualifying income before figuring their tax bill. For a sole proprietor in the 24% bracket, for example, excluding 20% of income from taxation would have the effect of lowering the tax rate to 19.2%.

The changes to the taxation of pass-through businesses are some of the most complex provisions in the new law, in part because of lots of limitations and anti-abuse rules. They're designed to help prevent gaming of the tax system by taxpayers trying to have income taxed at the lower pass-through rate rather than the higher individual income tax rate. For many pass-through businesses, for example, the 20% deduction mentioned above phases out for taxpayers with incomes in excess of $157,500 on an individual return and $315,000 on a joint return. At the end of the day, most individuals who are self-employed or own interests in partnerships, LLCs or S corporations will be paying less tax on their pass-through income than in the past. Read our article here-

Pass Thru Tax Reform

Meals and Entertainment

Given the new meals and entertainment landscape (and uncertainty) from the Tax Cuts and Jobs Act of 2017 (TCJA), we believe business owners need to be aware of the possible interpretations of the new rules. The Watson CPA Group subscribes to the Bradford Tax Institute's newsletters. Murray Bradford is a CPA and his articles are thought provoking, and at times a bit crazy. However, he usually provides tax code and references. His latest article on business meals is a great trip down memory lane to illustrate how we ended up where we did. Forbes and Fortune, and other internet writers rarely reference tax code and committee reports so stay away from those types.

As mentioned elsewhere, the Watson CPA Group believes that having lunch with a client or prospect has always been considered entertainment. And… the fact that the entertainment was over a meal does not make the meal deductible- it made the cost of entertainment, which included a meal, deductible. Now that entertainment deductions are gone, our contention is that meals with clients and prospects are also gone.

Having said that, we are not interested in fighting with our clients about how to carry the 1 when faced with unclear tax code- if the code remains unclear come next year, then we will error on the side of client advocacy. In other words, it is not the taxpayer's fault that Congress and box of crayons can't write a law in which a 5th grade should be able to read.

Meals & Entertainment Article

Moving Expenses

The new law eliminates a popular deduction for moving expenses. The deduction, which was available to itemizers and non-itemizers, allowed taxpayers to deduct the cost of a job-related move. Going forward, only members of the military can claim it.

ACA Penalty

The new law does repeal the “individual mandate” – the requirement that demands that you have health insurance or pay a fine. But not until 2019. For 2018, the mandate is still in place.

529 to Pay for High School

The new law allows families to spend up to $10,000 a year from tax-advantaged 529 savings plans to cover the costs of K-12 expenses for a private or religious school. Previously, tax-free distributions from those plans were limited to college costs.