<u>Highlights of Tax Cuts and Job Acts (“the TCJA“)</u>

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2018 brings a major change to the Internal Revenue Code. The Tax Cuts and Jobs Act (TCJA) include permanent changes to the tax code as well as many temporary changes. Regardless of your income bracket it is very likely the TCJA will impact you in 2018 and the years that follow.

The following are the most important changes of the new law that have an impact on individuals. Keep in mind that some of the changes are only effective for tax years beginning in 2018 through 2025.

<u>Tax Rates</u>: The number of tax brackets (7) remains unchanged, however the amount of income that is taxed within each bracket has changed. The new tax brackets beginning in 2018 area as follows:

- 10%: Single taxpayers with incomes between $0 and $9,525; married couples filing jointly with incomes between $0 and $19,050.
- 12%: Single taxpayers with incomes between $9,525 and $38,700; married couples filing jointly with incomes between $19,050 and $77,400.
- 22%: Single taxpayers with incomes between $38,700 and $82,500; married couples filing jointly with incomes between $77,400 and $165,000.
- 24%: Single taxpayers with incomes between $82,500 and $157,500; married couples filing jointly with incomes between $165,000 and $315,000.
- 32%: Single taxpayers with incomes between $157,500 and $200,000; married couples filing jointly with incomes between $315,000 and $400,000.
- 35%: Single taxpayers with incomes between $200,000 and $500,000; married couples filing jointly with incomes between $400,000 and $600,000.
- 37%: Single taxpayers with incomes of $500,000 or more; married couples filing jointly with incomes of $600,000 or more.

<u>Standard deduction.</u> The standard deduction is increased to $24,000 for married couples filing jointly and $12,000 for singles and married taxpayers filing separately. Because of the larger standard deduction many taxpayers will no longer itemize their deductions. These figures will be indexed for inflation after 2018. The increase in the standard deduction is temporary and unless Congress changes the law this provision will end in 2025.

Exemptions. The new law suspends the deduction for personal exemptions. Thus, starting in 2018, taxpayers can no longer claim personal or dependency exemptions.

Child and family tax credit. The new law increases the credit for qualifying children (i.e., children under 17) to $2,000 from $1,000 of which $1,400 is refundable. It also introduces a new (nonrefundable) $500 credit for a taxpayer's dependents who are not qualifying children. The adjusted gross income level at which the credits begin to be phased out has been increased to $200,000 ($400,000 for joint filers).

State and local taxes. The amount tax payers can deduct for state and local income and property taxes is limited to a total of $10,000 starting in 2018.

Mortgage interest. Mortgage interest on loans used to acquire a principal residence and a second home is only deductible on debt up to $750,000, starting with loans taken out in 2018. Previously up to $1 million in mortgage interest was deductible. Beginning in 2018 there is no longer any deduction for interest on home equity loans, regardless of when the debt was incurred.

Miscellaneous itemized deductions. There is no longer a deduction for miscellaneous itemized deductions. Previously these expenses were deductible to the extent they exceed 2 percent of adjusted gross income. Miscellaneous itemized deductions were items that included investment management fees, tax preparation costs, unreimbursed employee expenses and union dues. This deduction is suspended from 2018-2025.

Medical expenses. For most taxpayers medical expenses were deductible only to the extent they exceeded 10 percent of adjusted gross income. In 2017 and 2018, medical expenses are deductible to the extent they exceed 7.5 percent of adjusted gross income for all taxpayers.

Overall limitation on itemized deductions. The new law suspends the overall limitation on itemized deductions that formerly applied to taxpayers whose adjusted gross income exceeded specified thresholds (commonly known as the Pease limitation). The itemized deductions of such taxpayers were reduced by 3% of the amount by which AGI exceeded the applicable threshold, but the reduction could not exceed 80% of the total itemized deductions, and certain items were exempt from the limitation.

Moving expenses. Most taxpayers will no longer be able to deduct job-related moving expenses.

Alimony. Beginning in 2019, alimony will no longer be deductible by the paying spouse and will not be taxable to the receiving spouse. This provision does not apply to existing divorce decrees and separation agreements or divorces and separation agreements that are executed before January 1, 2019.

Health care "individual mandate."" Starting in 2019, there is no longer a penalty for individuals who fail to obtain minimum essential health coverage.

Estate and gift tax exemption. Effective for decedents dying, and gifts made, in 2018, the estate and gift tax exemption has been increased to roughly $11.2 million per person ($22.4 million for married couples).

Change to 529 Plans For the first-time taxpayers may use 529 plan assets to pay for tuition in connection with enrollment at an elementary or secondary public, private, or religious school. Thus, tax-free distributions from 529 plans can now be received by beneficiaries who pay these expenses, effective for distributions from 529 plans after 2017. The amount of cash distributions from all 529 plans per single beneficiary during any tax year cannot exceed $10,000 for elementary school and secondary school tuition incurred during the tax year. There is no such limitation when 529 accounts are used for college expenses.

Recharacterization of IRA contributions. Prior to TCJA an individual who funded (either a contribution or conversion) of a Roth IRA had the opportunity to change their mind and undo the transaction without any tax penalty. Beginning in 2018 individuals no longer can undo a contribution or conversion to a Roth IRA.

Alternative minimum tax (AMT) exemption. The AMT has been retained for individuals by the TCJA but the exemption has been increased to $109,400 for joint filers ($54,700 for married taxpayers filing separately), and $70,300 for unmarried taxpayers. The exemption is phased out for taxpayers with alternative minimum taxable income over $1 million for joint filers, and over $500,000 for all others.

Casualty and theft losses. The itemized deduction for casualty and theft losses has been suspended except for losses incurred in a federally declared disaster area.

New deduction for "qualified business income." TCJA included a new deduction for owners of “pass-through” business entities such as partnerships, S corporations, LLCs and sole proprietorships. The provisions of this new deduction are very complex, and it is important to seek advice from your tax professional to determine eligibility and applicability.

In general beginning in 2018, taxpayers in these “pass-through” entities are allowed a deduction equal to 20 percent of "qualified business income." To be eligible for the deduction the income must be from a trade or business within the U.S. Income from investments such as dividends, interest and capital gains do not qualify. Amounts received as compensation from the business also does not quality. For taxpayers with taxable income above $157,500 ($315,000 for joint filers), (1) a limitation based on W-2 wages paid by the business is phased in, and (2) income from the following trades or businesses is phased out of qualified business income: health, law, consulting, athletics, financial or brokerage services, or where the principal asset is the reputation or skill of one or more employees or owners.