JVL Associates, LLC
Bonus Edition

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The Tax Cuts and Jobs Act of 2017

After a long and contentious process, President Trump signed *The Tax Cuts and Jobs Act of 2017* on December 22, 2017. The Act is 1097 pages long, covering changes for Individuals, Estates, Businesses, Pass-Through Entities and Corporations. The following is a brief recap of some of the more common provisions in the Act.

INDIVIDUALS:

1) All Individual tax provisions sunset on December 31, 2025. This is a result of the procedural way the Act was moved through Congress – through the budget reconciliation process which does not require 60 votes in the U.S. Senate.

2) While the Act does not repeal the "Individual Mandate" of the Affordable Care Act it reduces the penalty for not obtaining insurance to $-0- beginning January 1, 2019. Thus, for all practical purposes, individuals can choose to be uninsured without fear of penalty.

3) The standard deductions for 2018 have been increased as follows:

Married Filing Joint	$24,000 up from $12,700 in 2017
Married Filing Separate	$12,000 up from $ 6,350 in 2017
Head of Household	$18,000 up from $ 9,350 in 2017
Single	$12,000 up from $ 6,350 in 2017

The standard deduction is an alternative to itemizing deductions and therefore the result is that fewer people will need to itemize their deductions, thus simplifying many tax returns.

4) The Act eliminates the personal and dependent exemption deductions ($4,050 in 2017) and replaces them by expanding the Child & Family Credits (see #8 below). While individual cases will vary, the goal is that the increase in the standard deduction (item #3) will offset the loss of the personal exemption for individuals / couples without children and that the expansion of the Child Credit will offset the loss of the dependent exemption for individuals / couples with children.

5) Changes to itemized deductions:

   A) Medical expenses are deductible to the extent they exceed 7.5% of AGI in 2017 and 2018. The floor reverts to 10% of AGI in 2019.

   B) All state and local taxes, including property taxes, are limited to $10,000 beginning 2018.

C) Home mortgage interest deduction is limited to $750,000 of "acquisition debt" for homes purchased after 12/15/2017. All mortgage debt prior to that date is grandfathered in.

D) Home equity line of credit (HELOC) interest is no longer deductible unless the proceeds are used for "acquisition debt" or major capital improvements. The HELOC balance is included in the new $750,000 limitation.

E) Charitable deductions are deductible against 60% of AGI, up from 50% in 2017.

F) Casualty losses will only be allowed if the loss is related to a "disaster" as declared by the President of the U.S. under the Disaster Relief and Emergency Assistance Act.

G) All "Tier II" miscellaneous itemized deductions are eliminated, including:

i) Unreimbursed employee business expenses, including home office deductions

ii) Tax preparation fees

iii) Legal, professional, investment related expenses, not pertaining to a business

iv) Union dues, uniforms, special work-related clothing

H) The Itemized Deduction Phase Out (Pease Limit) has been eliminated.

6) Tax brackets were widened, thereby subjecting more taxable income to the lower tax rates. For example, the Married Filing Joint taxable income brackets were changed as follows:

Bracket 1 taxable income	$19,050 in 2018 from $ 18,650 in 2017
Bracket 2 taxable income	$77,400 in 2018 from $ 75,900 in 2017
Bracket 3 taxable income	$165,000 in 2018 from $153,100 in 2017
Bracket 4 taxable income	$315,000 in 2018 from $233,350 in 2017
Bracket 5 taxable income	$400,000 in 2018 from $416,700 in 2017
Bracket 6 taxable income	$600,000 in 2018 from $470,700 in 2017
Bracket 7 taxable income	Excess over Bracket 6

7) Tax rates were also reduced, as follows:

Bracket 1 tax rate	no change at 10%
Bracket 2 tax rate	12% in 2018 from 15% in 2017
Bracket 3 tax rate	22% in 2018 from 25% in 2017
Bracket 4 tax rate	24% in 2018 from 28% in 2017
Bracket 5 tax rate	32% in 2018 from 33% in 2017
Bracket 6 tax rate	35% in 2018 from 35% in 2017
Bracket 7 tax rate	37% in 2018 from 39.6% in 2017

8) Child & Family Credits:

   A) Increases the Child Tax Credit to $2,000 – up from $1,000 in 2017

   B) The first $1,400 of the Child Tax Credit is refundable – subject to Income Limit Phase Outs

   C) Establishes a $500 non-refundable credit for other qualifying dependents

9) The Kiddie tax for children with unearned income was changed from using their parents' tax rates to using Trust & Estate tax rates.

10) The Alternative Minimum Tax (AMT) was retained for individuals but both the exemption and phase out provisions were increased which should reduce the number of filers subject to the tax.

11) Section 529 plans were expanded to allow for payment of qualifying educational expenses for K-12 education, including private and parochial schools.

12) Beginning for divorce decrees entered into after 2018, alimony will no longer be deductible by the payer, nor be taxable income to the recipient. Divorce decrees entered into prior to January 1, 2019 will be unaffected – no change to the current tax structure.

13) Moving expenses will no longer be deductible and employer reimbursed moving expenses will be included in the employee's income. There is an exception for military personnel.

14) Achievement awards and transportation fringe benefits (ex. Transit passes) will no longer be tax free to the recipient.

ESTATES:

While the estate tax was not eliminated the exemption was doubled – from $5,490,000 in 2017 to $11,200,000 in 2018. Thus, a married couple will not incur estate taxes unless their combined estate is worth more than $22,400,000. The step up in basis to Date of Death values was retained, so inheritors will receive the assets at the value as of the deceased's date of death.

The same exemptions apply to Gift Tax and Generation Skipping Tax transfers.

BUSINESSES:

1) The Act allows the full expensing of business assets acquired between 9/28/2017 and 12/31/2022. Beginning in 2023 a 20% phase-down schedule kicks in, reducing the percentage allowed to be expensed in the year acquired. The expensing does not apply to real property.

2) The luxury auto limits were expanded to allow a faster depreciation deduction for higher cost business vehicles.

3) Business interest expense is limited to 30% of EBITDA (earnings before interest, taxes, depreciation and amortization) for certain businesses with average gross receipts greater than $25 million. Most real estate entities are exempt from this limitation.

4) Business entertainment (tickets to events, membership dues, etc.) is no longer deductible.

5) Certain business credits have been repealed, including employer provided child care.

PASS-THROUGH ENTITIES:

The Act provides for a 20% deduction for certain pass-through business income. This is the business income that is taxed on the owner's individual tax return from Sole Proprietorships, Partnerships, Sub-chapter S Corporations and LLC's. The deduction does not reduce AGI, instead it reduces taxable income which is calculated after deducting the standard deduction or itemized deductions. However, for single taxpayers with taxable income over $157,500 or married filing joint taxpayers with taxable income over $315,000 (applicable thresh-holds) a different set of rules apply.

1) For taxpayers with taxable income under the applicable thresh-holds the deduction is computed as the lesser of:

    A) 20% of "Qualified Business Income" or,

    B) 20% of the taxpayers' taxable income (with certain adjustments)

2) For taxpayers with taxable income exceeding the applicable thresh-holds, the 20% pass-through deduction is either phased out (single taxpayers between $157,500 - $207,500 and married filing joint taxpayers between $315,000 - $415,000) or completely eliminated if the taxpayer is engaged in a "specialized trade or business". "Specialized trade or businesses" are those where personal services are the major driver of the business income. Examples include health services (doctors, dentists, etc.), law, accounting, actuarial services, performing arts, consulting, athletics, financial services, brokerage services, or any business where the principal asset of the business is the reputation or skill of one or more of the employees.

3) For taxpayers with taxable income exceeding the applicable thresh-holds but are not engaged in a "specialized trade or business" the 20% pass-through deduction computed under 1 above is subject to an additional test and may not exceed the greater of:

    A) 50% of the wages paid by the business or,

    B) 25% of the wages paid by the business plus 2.5% of the unadjusted tax basis of the depreciable property owned by the business

The goal of this provision is to bring the tax rate on "Qualified Business Income" from a pass-through entities more in line with the new reduced corporate tax rate. Then reason for the "specialized trade or business" income provision is to prevent business owners from playing games between earnings from services performed and income from a trade or business. While complicated, the provisions should reduce the tax rates on most business income generated by a non personal-service trade or business.

CORPORATIONS:

All of the tax provisions relating to corporations are permanent, there is no sunset time line for them.

1) Creates flat tax rate of 21% - currently graduated rates up to 35%.

2) Moves the U.S. to a "territorial system". Income is taxed in the country where the income is generated.

3) Allows for a reduced rate on repatriated earnings back to the U.S. The rate for cash assets is 15.5% and illiquid assets is 8%.

The reduction in the corporate tax rate moves the U.S. from one of the highest taxed countries to one of the lowest. The goal is to make the U.S. the most attractive place in the world to conduct business. The repatriation tax rates are intended to incentivize companies to bring their foreign earnings back into the U.S. for investment here.

The Tax Cuts and Jobs Act of 2017 is the most sweeping change to the U.S. tax code since the 1980's. One side of the aisle believes it is critical to spurring future growth in the U.S. economy, while the other side of the aisle has called it "Armageddon". Only time will tell.

At JVL Associates, we believe taxes are an important part of the financial planning process. Although we do not prepare tax returns, we work closely with our clients and their tax professionals, and we encourage you to talk with your tax professional as to how the new Act affects your particular tax situation.

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