JVL Associates, LLC NEWSLETTER

March 2018

2018 Taxes

By now, most of us have filed our 2017 tax returns and turned our focus to spring and the upcoming summer. But, before you put taxes in the rearview mirror you should consider that your 2017 return is the last return you will file under a long-standing set of tax rules, and your 2018 tax return will be the first year you file under the new Tax Cuts and Jobs Act of 2017.

So, what should we know for 2018?

Saving for Retirement Continues to be Incentivized Under the New Tax Act:

Maximum Contribution

$18,500
$24,500 over age 50

If your employer maintains a ***401k, 403b or 457 plan*** you should continue to take advantage of this benefit. The amount you contribute to the plan through your payroll withholding continues to be tax deductible, thus reducing your tax bill. The maximum amount an employee can contribute for 2018 is $18,500 ($24,500 if over age 50). Since many employers offer a matching amount to incentivize savings, the amount added by your employer not only adds to the "return" on your contributions it is free of current tax and thus grows tax deferred until you withdraw the funds during your retirement.

Individual Retirement Account (IRA) rules did not change. For persons not covered by an employer provided retirement plan there are no income restrictions on making tax deductible IRA contributions. For persons that are covered by an employer provided retirement plan, the tax deduction is reduced if their income exceeds $101,000 (married filing jointly) or $63,000 (single taxpayer).
The amount a person is allowed to contribute to their IRA for 2018 remains at $5,500 ($6,500 if over age 50).

Maximum Contribution

$5,500
$6,500 over age 50

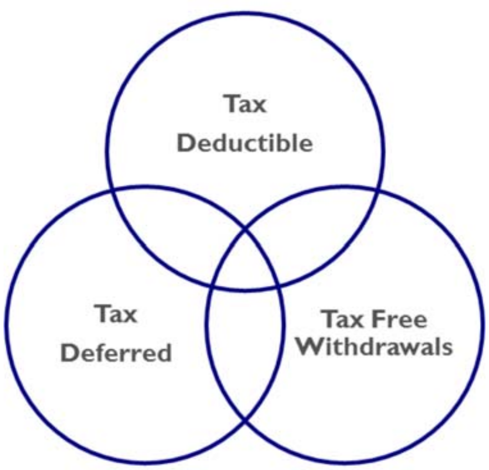
Roth IRA's continue to be available to persons with incomes under $189,000 (married filing jointly) or $120,000 (single taxpayer), regardless of their participation in an employer provided retirement plan. While the contributions are not currently tax deductible, the income earned is free from tax in the year of withdrawal. It is one of the very few vehicles that allows a total exemption of your earnings from taxation.

Roth Conversions continue to be a great way to fill a tax bracket "bucket" with additional income, thereby taking advantage of lower tax rates in certain years. In certain cases, it may make sense to convert a portion of your after-tax IRA to a Roth IRA, thus intentionally creating taxable income, to offset certain tax deductions or to make maximum use of the lower tax brackets. There are no income restrictions so anyone can utilize this strategy. However, new for 2018, is that once the conversion takes place it cannot be undone – thus making planning very important. This requires a solid knowledge of your current year taxable income and the respective tax brackets applied to that income.

Back-door Roth IRA contributions were given Congress's "blessing" in the new Tax Act. This is a strategy that allows persons who cannot make a Roth IRA contribution due to income limitations (see above) to make a nondeductible traditional IRA contribution and then convert it to a Roth IRA before any earnings accrue. By doing this, there are no current income tax effects, yet the Roth IRA grows tax free. This strategy has one caveat - if you have any existing traditional IRA accounts, the tax law requires a proration of the amount converted – thus reducing the tax benefits in situations where you have a traditional IRA already in place.

There are two requirements for any of the IRA strategies described above - the person must be under age 70.5 and have earned income equal to or greater than the amount of the IRA contribution.

Health Savings Accounts (HSA) continue to be one of the best tax benefits in the tax code. Contributions to HSA's are tax deductible, earnings grow tax deferred and withdrawals used for qualified medical expenses are free from tax. This makes HSA's better than any retirement plan benefit described above. Tax deductible going in plus tax free coming out! The maximum amount a person can contribute for 2018 is $6,850 (family coverage) or $3,450 (self-only coverage).



In order to contribute to an HSA, one must be covered under a high deductible health plan (HDHP), cannot be covered by Medicare and must not be claimed as a dependent on someone else's tax return. A HDHP must have a minimum annual deductible limit of $2,700 (family coverage) or $1,350 (self-only coverage) and maximum annual deductible plus other out of pocket limit of $13,300 (family coverage) or $6,650 (self-only coverage). This covers a lot of health plans today.

To take maximum advantage of this tax benefit, a person could make the maximum annual contributions, self-fund their annual medical expenses thereby allowing the HSA to grow tax deferred and wait as long as possible before taking withdrawals. Medicare premiums are a qualified medical expense thus enabling a person to take tax free withdrawals during retirement.

Changes to Itemized Deductions & Child Credit:

The Tax Cuts and Jobs Act made major changes to both the standard deduction (available to all tax filers) and to specific itemized deductions (available to those who choose to itemize their deductions on Schedule A). The purpose of these changes was to simplify the tax filing process. It is estimated that the changes will result in 90% of all tax returns being able to utilize the standard deduction, up from 70% of all tax returns today.

Standard Deduction **-** The standard deduction for 2018 is increased to $24,000 for married filing jointly ($12,700 in 2017) and $12,000 for single filers ($6,350 in 2017). This is the deduction you are allowed to claim against your adjusted gross income regardless of the amount you actually spent during the year on qualifying itemized deductions (see below). If the combination of your itemized deductions exceeds this standard deduction, you can choose to use the itemized deduction method.

Standard Deduction
$12,000 – Single
$24,000 – MFJ

A big change for 2018 is that the standard deduction now replaces both the standard deduction and the personal and dependent exemption ($4,050 per person / dependent). Thus, you are no longer able to claim the personal and dependent exemption in addition to your standard deduction / itemized deductions.

Medical Expenses – the definition of medical expenses has not changed but the Act did modify the amount that are deductible. For 2018, medical expenses are deductible to the extent they exceed 7.5% of a taxpayers' Adjusted Gross Income (AGI), the same as in 2017. However, in 2019, the threshold increases to 10% of AGI. To see if this will affect you, look at your 2017 tax return, Schedule A, lines 1 – 4.

$10,000
Maximum
Deduction for
State and Local
Taxes

Taxes – this is by far the most sweeping, and thus controversial, change in the Tax Act. The maximum state and local taxes (SALT) deduction that can be claimed in 2018 is $10,000. This is the combination of property taxes, sales taxes, and state and city income taxes. To see if this affects you, look at your 2017 tax return, Schedule A, line 5 - 9. If line 9 is greater than $10,000 you will no longer be able to deduct the amount in excess of $10,000.

Mortgage Interest – the new Tax Act changes the amount of mortgage interest eligible for deduction in 2018. In 2017 you were allowed to deduct the interest paid on up to $1 million of a mortgage if used for "home acquisition debt" plus the interest paid on another $100,000 of a home equity loan, regardless of how the proceeds were used (amounts for married filing jointly).

However, starting in 2018, for new loans entered into after December 15, 2017 you will only be able to deduct the interest on up to $750,000 of "home acquisition debt" paid on a mortgage (amount is for married filing jointly). The interest on home equity loans entered into after December 15, 2017 is no longer deductible.

There is a grandfather provision for loans in effect as of December 16, 2017 covering "home acquisition debt". The interest on up to $1 million remains for a mortgage but the interest on $100,000 of home equity loans is deductible only if the proceeds can be traced directly to "home acquisition debt". Interest paid on the proceeds from an existing home equity loan that cannot be traced to "home acquisition debt" will no longer be deductible. "Home acquisition debt" is debt that is incurred to purchase, construct or substantially improve a primary or secondary residence and is secured by the residence.

Mortgage interest is reported on your Schedule A, lines 10 and 11. In order to determine if this affects you, you will need to know the amount and terms of your debts. For persons with a home equity line currently in place, it is important to understand and document the use of the proceeds to determine if that interest will be deductible in 2018. For persons looking to purchase a home in 2018, the $750,000 limit will apply.

Charitable Contributions **-** the Tax Act changed the allowable deduction for charitable contributions from 50% of Adjusted Gross Income (AGI) to 60%. Taxpayers will continue to be able to deduct charitable contributions that meet the substantiation rules. In order to be tax deductible a taxpayer must have a receipt for any contribution in excess of $250 from the donee organization stating whether any goods or services or anything of value were given to the donor. You should make sure all receipts meet this requirement, and if not contact them and ask them to provide you a corrected receipt.

Another change for 2018 is that contributions to an institution of higher learning will no longer be deductible if made in exchange for the right to purchase tickets to an athletic event. This has been a common practice for major university season ticket holders.

Your charitable contributions are recorded on Schedule A, line 16 – 19. Generous taxpayers who donate more than 50% of their AGI will see an increase in their 2018 deduction. Unused contributions carried forward to 2018 will also be able to be used to the extent of 60% of AGI.

Miscellaneous Deductions **-** the deductions for unreimbursed employee expenses, union dues, tax preparation fees, investment related fees and safe deposit box fees are no longer deductible in 2018. These expenses, in aggregate, were deductible to the extent they exceeded 2% of a person's Adjusted Gross Income. To determine if this change affects you look at your 2017 tax return, Schedule A, line 21 – 27.

Limit on Itemized Deductions – In 2017 the total amount of itemized deductions was reduced if the taxpayers' income exceeded $313,800 (married filing jointly). This limitation was eliminated in 2018. Now, all qualifying itemized deductions can be claimed as a deduction against your adjusted gross income.

Child Credit – Another major change for 2018 is the increased child credit. First, they doubled the credit amount to $2,000 of which $1,400 is refundable over and above the taxpayer's income tax. In addition, they raised the phase-out income level to $400,000 (married filing jointly) up from $110,000 in 2017 so more taxpayers will be able to benefit from the credit. The Act also created a $500 nonrefundable credit for certain qualifying non-child dependents.

SCHEDULE A (Form 1040)
Department of the Treasury Internal Revenue Service (99)

Itemized Deductions

▶ Go to *www.irs.gov/ScheduleA* for instructions and the latest information.
▶ Attach to Form 1040.
Caution: If you are claiming a net qualified disaster loss on Form 4684, see the instructions for line 28.

OMB No. 1545-0074
2017
Attachment Sequence No. 07

Name(s) shown on Form 1040 | Your social security number

Medical and Dental Expenses		**Caution:** Do not include expenses reimbursed or paid by others.		
	1	Medical and dental expenses (see instructions)	1	
	2	Enter amount from Form 1040, line 38 [2]		
	3	Multiply line 2 by 7.5% (0.075)	3	
	4	Subtract line 3 from line 1. If line 3 is more than line 1, enter -0-		4
Taxes You Paid	5	State and local **(check only one box):** a ☐ Income taxes, **or** b ☐ General sales taxes	5	
	6	Real estate taxes (see instructions)	6	
	7	Personal property taxes	7	
	8	Other taxes. List type and amount ▶	8	
	9	Add lines 5 through 8		9
Interest You Paid	10	Home mortgage interest and points reported to you on Form 1098	10	
Note: Your mortgage interest deduction may be limited (see instructions).	11	Home mortgage interest not reported to you on Form 1098. If paid to the person from whom you bought the home, see instructions and show that person's name, identifying no., and address ▶	11	
	12	Points not reported to you on Form 1098. See instructions for special rules	12	
	13	Mortgage insurance premiums (see instructions)	13	
	14	Investment interest. Attach Form 4952 if required. See instructions	14	
	15	Add lines 10 through 14		15
Gifts to Charity	16	Gifts by cash or check. If you made any gift of $250 or more, see instructions	16	
If you made a gift and got a benefit for it, see instructions.	17	Other than by cash or check. If any gift of $250 or more, see instructions. You **must** attach Form 8283 if over $500	17	
	18	Carryover from prior year	18	
	19	Add lines 16 through 18		19
Casualty and Theft Losses	20	Casualty or theft loss(es) other than net qualified disaster losses. Attach Form 4684 and enter the amount from line 18 of that form. See instructions		20
Job Expenses and Certain Miscellaneous Deductions	21	Unreimbursed employee expenses—job travel, union dues, job education, etc. Attach Form 2106 or 2106-EZ if required. See instructions. ▶	21	
	22	Tax preparation fees	22	
	23	Other expenses—investment, safe deposit box, etc. List type and amount ▶	23	
	24	Add lines 21 through 23	24	
	25	Enter amount from Form 1040, line 38 [25]		
	26	Multiply line 25 by 2% (0.02)	26	
	27	Subtract line 26 from line 24. If line 26 is more than line 24, enter -0-		27
Other Miscellaneous Deductions	28	Other—from list in instructions. List type and amount ▶		28
Total Itemized Deductions	29	Is Form 1040, line 38, over $156,900? ☐ **No.** Your deduction is not limited. Add the amounts in the far right column for lines 4 through 28. Also, enter this amount on Form 1040, line 40. ☐ **Yes.** Your deduction may be limited. See the Itemized Deductions Worksheet in the instructions to figure the amount to enter.		29
	30	If you elect to itemize deductions even though they are less than your standard deduction, check here ▶ ☐		

For Paperwork Reduction Act Notice, see the Instructions for Form 1040. Cat. No. 17145C **Schedule A (Form 1040) 2017**

Planning for the 2018 changes:

With the changes to itemized deductions coming into effect in 2018, you should determine whether you will be able to itemize this calendar year. If your deductions under the new rules are greater than $24,000, you will continue to use the itemized deduction method. But for those close to the threshold, there are planning opportunities available to you.

By "lumping" deductions where you control the timing of the payment, a taxpayer could alternate from the standard deduction in one year to the itemized deduction method the following year.

An example would be to pay three property tax bills in one year and one the next (subject to the overall limit of $10,000 of state and local tax deduction per year). Charitable contributions from two years could be "lumped" into one year. The goal would be to exceed the $24,000 standard deduction in one year and use the standard deduction the next. This strategy benefits you if the amount of your combined two-year tax deductions exceeds your combined two-year actual expenses.

Trade or Business Provisions:

Expensing of Business Assets – The Tax Act allows the full expensing of assets acquired and used in a trade or business in the year acquired. This applies to all trade and business enterprises regardless of how formed. For individuals this includes sole-proprietorships, partnerships, limited liability companies (LLC) and S-Corporations. Thus, the income reported by persons with flow-through income from one of these entities will be able to use the expense deduction against their taxable income.

Pass Through Business Income Deduction - Beginning with 2018 an individual will be able to reduce their trade or business income by 20%, subject to certain income limitations. For individuals with income reported on Schedule C or on Schedule E from flow-through entities like partnerships, LLCs or S-Corporations there will be an adjustment equal to 20% of the reported income. This adjustment reduces the amount of income subject to tax.

There are restrictions on the amount of the deduction for certain "specialized trade or businesses" if the taxpayer has taxable income over $315,000 (married filing jointly) or $157,500 (single filers). "Specialized trade or businesses" are those where personal services are the major driver of the business income. Examples are health services (doctors, dentists), law, accounting, actuarial services, performing arts, consulting, athletics, financial services, brokerage services, or any business where the principal asset of the business is the personal reputation or skill of one or more of the employees.

If you have income reported on Schedule C or Part II of Schedule E you may qualify for this deduction.

Tax planning is a vital part of managing your finances. At JVL Associates, LLC we take taxes seriously. Every dollar of tax savings is a dollar available for spending or investing the way you choose. We work closely with our clients and their tax preparers to make sure that all tax strategies are considered.

If you know of someone who could benefit from our services please pass our name along. We would enjoy sharing our experience with others.

All of our newsletters are archived on our website at www.jvlassociates.com.

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