

# The Tax Cuts and Jobs Act of 2017

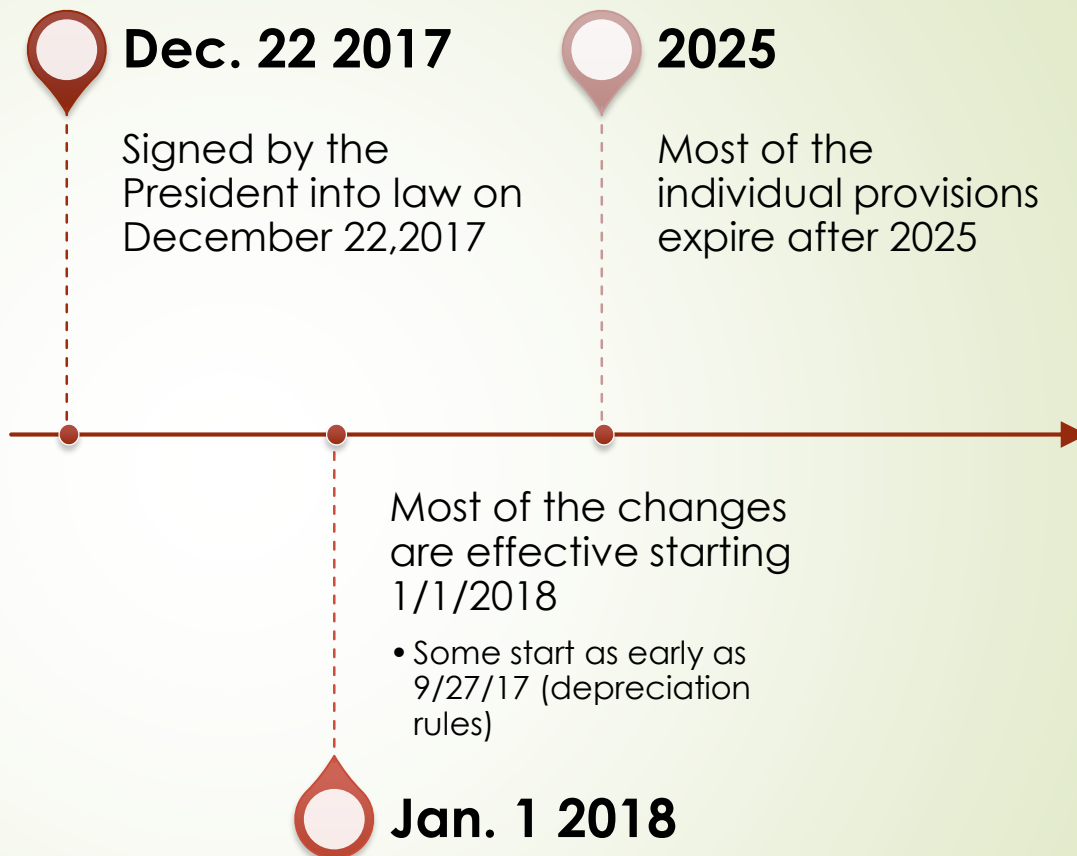
## What You Need to Know



Catherine Lightfoot, CPA, CHBC

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# Overview

- ▶ Changes affecting individuals:
  - ▶ New tax rates and brackets, increase in standard deduction, repeal of personal exemption
  - ▶ Increase in child tax credit, other credits modified
  - ▶ New limit on mortgage interest
  - ▶ Dollar limit on real estate, state and local and sales tax
  - ▶ Other changes to Schedule A
  - ▶ Alternative Minimum Tax improved
  - ▶ Adjustments to income modified or eliminated

## ► Changes affecting businesses:

- Reduction in corporate tax rates
- Increase bonus depreciation to 100% + Sec 179 to \$1m
- New deduction for sole proprietors and pass through business income
- Liberalize the rules for allowing the cash method of accounting
- Repeal the domestic production activities deduction

# Overview (cont.)

## ▶ **What didn't happen:**

- ▶ Repeal of Alternative Minimum Tax for individuals
- ▶ Repeal of Estate taxes
- ▶ Homestead exemption
- ▶ FIFO rule for stock sales
- ▶ Salary changes for S Corps and Partnerships
- ▶ Termination of contributions to medical savings accounts
- ▶ Inclusion of income tuition reduction programs
- ▶ Repeal of Work Opportunity Credit
- ▶ Eliminating credit for plug-in electric vehicles
- ▶ Repealing deduction for student loan interest
- ▶ Repealing completely Schedule A deduction for medical expenses
- ▶ Repeal of exclusion of interest from US Bonds used for higher education
- ▶ The additional Medicare tax is still here

# Overview (cont.)

## Individual Tax Brackets: Joint Returns and Surviving Spouse

Prior Law	2018	TCJA	2018
Taxable income	Rate	Taxable Income	Rate
\$0–\$19,050	10%	\$0–\$19,050	10%
\$19,050–\$77,400	15%	\$19,050–\$77,400	12%
\$77,400–\$156,150	25%	\$77,400–\$165,000	22%
\$156,150–\$237,950	28%	\$165,000–\$315,000	24%
\$237,950–\$424,950	33%	\$315,000–\$400,000	32%
\$424,950–\$480,050	35%	\$400,000–\$600,000	35%
Over \$480,050	39.6%	Over \$600,000	37%

*Adjusted for inflation after 2018*

## Kiddie Tax

Unearned income of children will be taxed at the tax rates for trusts:

Prior Law	2018	TCJA	2018
Unearned Income	Rate	Unearned Income	Rate
\$0–\$2,100	Child's rate	\$0–\$2,550	10%
Over \$2,100	Parents rates	\$2,550–\$9,150	24%
		\$9,150–\$12,500	35%
		Over \$12,500	37%

- No longer will it be allowed to include child's income on parents return
- Planning to avoid Kiddie Tax has become more important

## Individual Tax Brackets: Single

Prior Law	2018	TCJA	2018
Taxable income	Rate	Taxable Income	Rate
\$0–\$9,525	10%	\$0–\$9,525	10%
\$9,525–\$38,700	15%	\$9,525–\$38,700	12%
\$38,700–\$93,700	25%	\$38,700–\$82,500	22%
\$93,700–\$195,450	28%	\$82,500–\$157,500	24%
\$195,450–\$424,950	33%	\$157,500–\$200,000	32%
\$424,950–\$480,050	35%	\$200,000–\$500,000	35%
Over \$480,050	39.6%	Over \$500,000	37%

*Adjusted for inflation after 2018*



## Individual Tax Brackets: Head of Household

Prior Law	2018	TCJA	2018
Taxable income	Rate	Taxable Income	Rate
\$0–\$13,600	10%	\$0–\$13,600	10%
\$13,600–\$51,850	15%	\$13,600–\$51,800	12%
\$51,850–\$133,850	25%	\$51,800–\$82,500	22%
\$133,850–\$216,700	28%	\$82,500–\$157,500	24%
\$216,700–\$424,950	33%	\$157,500–\$200,000	32%
\$424,950–\$480,050	35%	\$200,000–\$500,000	35%
Over \$480,050	39.6%	Over \$500,000	37%

*Adjusted for inflation after 2018*

## Estates and Trusts – Tax Brackets

Prior Law	2018	TCJA	2018
Taxable income	Rate	Taxable Income	Rate
\$0–\$2,550	15%	\$0–\$2,550	10%
\$2,550–\$6,000	25%	\$2,550–\$9,150	24%
\$6,000–\$9,150	28%	\$9,150–\$12,500	35%
\$9,150–\$12,500	33%	Over \$12,500	37%
Over \$12,500	39.6%		

*Adjusted for inflation after 2018*

# Child Tax Credit - Increased

- ▶ Effective 1/1/2018-12/31/2025, Child Tax Credit amount increased to \$2,000 per child
- ▶ Phase out threshold amounts increased to \$400,000 for MFJ and \$200,000 for all other filers
- ▶ Credit increased to \$500 for each dependent that is not a “qualifying child”

# 529 Plans

- ▶ IRC 529(c)(7) – Elementary or secondary public, private, or religious school tuition considered “qualified higher education expenses.”
  - K-12 expenses capped at \$10,000 per year.
  - No cap for college tuition
- ▶ Rollover to ABLE accounts
- ▶ Discharge of student loans
  - ▶ Discharge due to death or disability not taxable income

## For years 2018-2025:

- \* Unified Estate and Gift Tax Exemption: \$10,000,000
  - \* Indexed for inflation after 2011 (\$11,200,000 for 2018).
  - \* Use of gift tax exemption during lifetime reduces estate tax exemption available at death.
  - \* Can still elect portability of deceased spouse's unused exemption amount.
- \* GST Tax Exemption: \$10,000,000
  - \* Indexed for inflation after 2011 (\$11,200,000 for 2018).
  - \* Automatic allocation rules for lifetime gifts to GST trusts.
  - \* 2018 annual gifting is \$15,000

# Estate Tax, Gift Tax, and GST Tax Exemption Amounts

# Changes for Retirement Plans

## **Roth IRA re-characterization rule repealed**

- Individuals will no longer be allowed to re-characterize a conversion of a traditional IRA to a ROTH IRA (cannot unwind a ROTH conversion)
- Individuals will still be allowed to re-characterize a contribution to a traditional IRA as a Roth contribution and vice versa

## **Rollover of Plan Loans**

- Employees will have until the due date for filing a return ( including extensions) to contribute loan balances to an IRA to prevent these amounts from becoming taxable upon termination

# Alimony Deduction

- Suspends above-the-line deduction for alimony payments
- Does not require that payee include alimony in income
  - Income used for alimony now taxed at payor's rate
- Effective for divorce decrees, separation agreements and certain modifications entered into after 2018

# Standard Deduction - changed Personal Exemption - eliminated

- ▶ Standard deduction raised to:
    - ▶ \$12,000 (for single and MFS)
    - ▶ \$18,000 (for Head of Household)
    - ▶ \$24,000 (for MFJ/SS)
    - ▶ Additional amount for blind or elderly:
      - ▶ Single \$1,600      Married \$1,300 each
  - ▶ Personal exemptions eliminated (i.e., \$4,050 in 2017)
    - ▶ In 2017, were subject to phase out rules
- \* effective 1/1/2018 - 12/31/2025



# Itemized Deductions

- ▶ Phase limitation on itemized deductions:
  - ▶ If AGI exceeds threshold amount, itemized otherwise allowable reduced by the lesser of:
    - ▶ 3% of the excess of AGI over the applicable amount; or
    - ▶ 80% of the amount of itemized deductions otherwise allowable
- ▶ For 2018 - 2025, this “Phase” limitation does not apply

# Medical Expense Deduction Temporary Threshold Reduction

- ▶ 1/1/2017 - 12/31/2018: Any taxpayer may deduct medical expenses to the extent they exceed 7.5% of AGI, instead of 10%
  - ▶ Retroactively extended reduction in floor (7.5% vs. 10%) through the end of 2018
  - ▶ Retroactively makes 7.5% floor available to any taxpayer during tax year 2017, regardless of age (do not have to be 65 years old)
  - ▶ Medical Deductions go back to 10% in 2019

# Individual Mandate

19

- Effective beginning in January 2019, no shared responsibility payment will be required
- No penalty will be imposed for failing to maintain minimum essential coverage

# Deduction of State and Local Taxes

- For 2018 - 2025, one \$10,000 aggregate limit for state and local taxes, e.g., property taxes, sales taxes and state (other than Texas) income tax
- IR-2017-210: IRS announces there is no current deduction for property taxes paid prior to being assessed
- § 164(b)(6): This \$10,000 limit should not apply to property taxes deducted as operating expenses for business and §212 activities (e.g., property reported on Schedule C and Schedule E)

# Residential Interest Expense

21

- Prior law: only the interest accruing and paid on the first \$1M of mortgage debt is deductible
- For personal residence mortgages in place after 12/15/2017 but before 1/1/2026, only the interest accruing and paid on the first \$750,000 (\$375,000 for MFS) of mortgage debt is deductible
- Refinanced debt is treated as incurred before 12/15/2017 to the extent the debt resulting from refinancing does not exceed the original debt amount

# Residential Interest Expense

- The \$1M and \$750,000 limits apply to the combined level of mortgage debt on personal residences (e.g., primary plus vacation)
- For 1/1/2018 - 12/31/2025, the interest deduction on home equity lines of credit is suspended

# Charitable Contributions

- Deductions allowed up to 60% of AGI (previously 50%) for cash donations to most charities
- Suspends 80% deduction for contributions made for university athletic seating rights

1/1/2018 - 12/31/2025: Loss of all miscellaneous itemized deductions subject to 2% floor

Tax Planning and tax advice

Investment management fees

Unreimbursed employee expenses

Tax tip – could you not be an employee?

Itemized  
Deductions  
\*eliminated



# Moving Expenses

25

- Effective 1/1/2018 - 12/31/2025, the above-the-line deduction of moving expenses is suspended, except for active duty military moving pursuant to military order and incident to a permanent change of station
- Effective 1/1/2018 - 12/31/2025, exclusion from income for qualified moving expense reimbursement suspended, except for active duty military moving pursuant to military order and incident to a permanent change of station

# Casualty Loss Deduction

26

- ▶ Effective 1/1/2018 – 12/31/2025, a personal casualty loss is only deductible if that loss occurred in a Federally declared disaster area
  - ▶ Taxpayer can increase the standard deduction by losses in excess of \$500
  - ▶ Penalty free distributions allowed from retirement plans up to \$100K for 2016 (2017 was not mentioned)
    - ▶ Income can be spread over 3 years

# What changed on Schedule A?

## SCHEDULE A (Form 1040)

Department of the Treasury  
Internal Revenue Service (99)

Name(s) shown on Form 1040

## Itemized Deductions

► Go to [www.irs.gov/ScheduleA](http://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

Your social security number

<b>Medical and Dental Expenses</b>	<b>Caution:</b> 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		
<b>Taxes You Paid</b>	5 State and local (check only one box):	5				
	a <input type="checkbox"/> Income taxes, or					
	b <input type="checkbox"/> General sales taxes					
	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	
<b>Interest You Paid</b>	10 Home mortgage interest and points reported to you on Form 1098	10				
	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				
	<b>Note:</b> Your mortgage interest deduction may be limited (see instructions).					
	12 Points not reported to you on Form 1098. See instructions for special rules	12				
	13 Reserved for future use	13				
	14 Investment interest. Attach Form 4952 if required. See instructions	14				
15 Add lines 10 through 14				15		
<b>Gifts to Charity</b>	16 Gifts by cash or check. If you made any gift of \$250 or more, see instructions.	16				
	17 Other than by cash or check. If any gift of \$250 or more, see instructions. You <b>must</b> attach Form 8283 if over \$500	17				
	18 Carryover from prior year	18				
	19 Add lines 16 through 18				19	
<b>Casualty and Theft Losses</b>	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	
<b>Job Expenses and Certain Miscellaneous Deductions</b>	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	
<b>Other Miscellaneous Deductions</b>	28 Other—from list in instructions. List type and amount ►				28	
<b>Total Itemized Deductions</b>	29 Is Form 1040, line 38, over \$156,900?					
	<input type="checkbox"/> <b>No.</b> 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.					
	<input type="checkbox"/> <b>Yes.</b> Your deduction may be limited. See the Itemized Deductions Worksheet in the instructions to figure the amount to enter.					
	30 If you elect to itemize deductions even though they are less than your standard deduction, check here					

# Net Operating Losses

28

- ▶ For NOLs arising in tax years ending after 12/31/2017:
  - ▶ NOL deduction limited to 80% of taxable income (determined without regard to such NOL)
  - ▶ Example: A has \$120 NOL in 2018 that is carried forward to 2019. In 2019, A has \$100 of taxable income. The NOL carryforward can only offset \$80 of 2019 taxable income and has taxable income of \$20
  - ▶ The remaining \$40 NOL is carried forward until it is used.

# Net Operating Losses

- ▶ For most taxpayers, carry back is repealed, but NOLs can be carried forward indefinitely
  - ▶ Terminate on death, but under § 1.642(h)-1, trust losses may flow to beneficiary
- ▶ Exception:
  - ▶ 2 year carryback for farming trade or business (defined in §263A(e)(4))
  - ▶ Old NOLs don't have the same 80% limitation for carryover

# A New Loss Limitation

30

- Net business losses in excess of \$500,000 joint (\$250,000 for others) are not allowed, but instead are treated as an NOL carryover
- For all noncorporate taxpayers
- The provision applies after the application of the passive loss rules



A, an unmarried taxpayer, owns a 25% interest in a LLC taxed as a partnership. A is a member manager of the LLC. In Year 1, A's distributive share of loss is \$600,000.

A is only able to deduct \$250,000 and the remaining \$350,000 is carried forward as an NOL.

## Example 1:

A, is married and spouse earns \$600,000 on a W-2. Year 1 A is allocated \$600,000 loss from LLC.

A is only able to deduct \$500,000 from LLC and remaining \$100,000 goes to NOL.

## Example 2:



- ▶ Assume a start up technology company expects to generate significant losses in the early years and the business plan envisions a sale of the company in a short time after they turn a profit.
- ▶ Might consider operating as a C Corporation, especially if the owners can utilize the qualified small business stock gain exclusion.

## New Consideration

- ▶ In general, the new law adds an extra deduction equal to 20% of the combined QBI (net profits) from all businesses owned by an individual.
- ▶ The deduction is limited by the greater of
  - ▶ 50% of W-2 wages paid by the business or
  - ▶ 25% of W-2 wages paid plus 2.5% of unadjusted basis of qualified property
- ▶ The “wage” rule does not apply if taxable income on the 1040 is less than \$157,500 (\$315,000 joint)
- ▶ The limitation phases in as taxable income increases by \$50,000 (\$100,000) over the above and is gone at \$415,000 for joint and \$207,500 for others.

## New Deduction for Qualified Business Income for Individuals [QBI]

- ▶ Income from self employment
- ▶ Income from S Corporations and Partnerships
- ▶ Certain dividends of REITs
- ▶ Patronage dividends
- ▶ Qualified publicly traded partnership income

## What is QBI?

- ▶ Dividends
- ▶ Interest Income
- ▶ Capital gains or losses
- ▶ Payment for reasonable compensation received from an S Corporation
- ▶ Guaranteed Payments for services from a partnership
- ▶ Foreign business income

QBI does  
**NOT**  
include:

## Income limitations

The wage limitation does not apply if taxable income is less than \$157,500 (\$315,000 for a joint return)

The limitation phases in as taxable income increases by \$50,000 (\$100,000 on a joint return) and is fully applied at \$207,500 and \$415,000 (joint).

Specified service trade or business is subject to both limitations.

Health, law, consulting, athletics, financial services, brokerage services, or any trade or business where principal asset is the reputation of people.

- ▶ Married TP with QBI of \$500,000. Wage allocation is \$100,000. TP's spouse has salary income of \$150,000. So, joint taxable income is \$650,000.
- ▶ The deductible amount is equal to the lesser of:
  - ▶ 20% of QBI (\$100,000) or
  - ▶ The greater of 50% of allocable share of wages (\$50,000) or 25% (\$25,000) of wages plus 2.5% of unadjusted basis of depreciable property (\$0).
  - ▶ Here the deductible amount is \$50,000
- ▶ TP's joint taxable income is \$650,000 less the \$50,000 deduction, or \$600,000.

## Example 1:

- ▶ Allocable share of wages is \$275,000
- ▶ Deduction is lessor of
  - ▶ 20% QBI (\$100,000)
  - ▶ 50% of wages: \$137,500
  - ▶ Deduction is \$100,000

## Example 1: (revisited)

- ▶ “Joe electrician” has a Sole Proprietorship and earns \$150,000. His wife is a teacher and earns \$75,000.
- ▶ Taxable income is \$150,000 + \$75,000 less SE tax \$11,475 = \$213,525 – no wage limitation
- ▶ QBI is \$30,000

## Example 2: (revisited)



- ▶ There is no change for the imposition of Self Employment Tax
- ▶ Reasonable Compensation will still be necessary for S Corporations – might be better to pay more
- ▶ Still have double tax issue with Corporations
  - ▶ 21% tax rate
  - ▶ Dividends to shareholders taxed at 20% + additional 3.8% Medicare Tax
  - ▶ Result is a net rate of 39.8% = 21% (79% x 23.8%)

# Planning in Light of New 199A Deduction

- ▶ C Corporation Tax Rates – no more brackets – 21% new rate, old rate as high as 35%
- ▶ Personal Service Corporations will also be taxed at a flat rate of 21%.
- ▶ Effective for tax years beginning after 2017

# C Corporation Tax Rates

- ▶ 100% Bonus Depreciation
  - ▶ Acquired and placed in service after 9/27/2017 and before 1/1/2023
    - ▶ 2023 – 80%                      2024 – 60%
    - ▶ 2025 – 40%                      2026 – 20%
    - ▶ 2027 and after none
    - ▶ Used property now qualifies

# Cost Recovery

- ▶ \$500,000 expense increases to \$1,000,000
- ▶ Allows 179 for subsequent improvements to commercial property for roofs, heating and A/C, fire protection, alarm systems, and security systems after 2017.
- ▶ Allows for 179 on personal property to furnish lodging – beds, furniture, appliances, etc.
- ▶ Maximum for SUVs > 6000 lbs remains at \$25,000.

## Section 179 Expensing

## Luxury Automobiles

- The Act increases the limits for deductions for luxury autos placed in service after 2017 as follows:

Period	2017	TCJA
First year	\$3,160	\$10,000
Second year	\$5,100	\$16,000
Third year	\$3,050	\$9,600
Fourth and later years	\$1,875	\$5,760

- These higher amounts are not available if bonus depreciation of \$8,000 is claimed

# Entertainment and Meals

- Effective 1/1/2018, expenses for entertainment, amusement, or recreation are completely nondeductible unless allowed under § 274(e)
- Examples of expenses deductible under § 274(e) include:
  - expenses treated as compensation to an employee;
  - expenses for entertainment sold to customers; and
  - expenses for recreational activities primarily for the benefit of the taxpayer's employees.

# Entertainment and Meals

- Meals: 50% of food and beverage expenses associated with trade or business are still deductible (e.g., meals consumed by employees on work travel)
- Expenses for employer-operated eating facilities are 50% deductible through 2025, then completely nondeductible



# Catherine Lightfoot, CPA Director of Healthcare

Catherine.Lightfoot@ECPB.com

<http://www.ECPB.com>



**ECPB** P.C.  
CPAs & BUSINESS ADVISORS

2950 North Loop West, Suite 1200  
Houston, Texas 77092  
Telephone: (713) 622-0016  
Facsimile: (713) 622-5527

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