# What does the Tax Cuts and Jobs Act mean to you?

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The Tax Cuts and Jobs Act, affectionately known as TCJA, has been one of the most controversial and sweeping such legislation in the recent past.  The objectives of the Act, as stated, was to provide tax reductions for American lower income taxpayers, provide relief for corporations in an effort to attract business back to the United States and a simplification of the tax system.  Effects of the Act are estimated to cost on the order of 1.5 trillion dollars over the next ten years.  This is expected by its lawmakers, to be recouped by a resurgence of the economy and additional jobs, resulting in more tax revenues from higher business volume and taxpayer incomes. There are many parts to the legislation, and the IRS is still sorting out regulations. Meaning, how it will all be put into practice.  This article attempts to sort what effects it will have on different taxpayers.

The most significant elements of the Act to taxpayers has been:

1. Reduction in tax rates in most **individual brackets**, and other changes in preparing taxes
2. A ‘pass-through’ income exemption for **self-employed individuals** and those participating in partnerships and Subchapter S Corporations.
3. An elimination of the **Alternative Minimum Tax** at the corporate level, and reduced applicability of AMT to individuals.

How TCJA will affect individual taxpayers

Many of the provisions affecting individual taxpayers “Sunset” or reverse to their original rules in the year 2025, but many expect that will be extended by new lawmakers by that time.

The most obvious changes in how taxes are prepared for individuals, is the elimination of **dependent ‘exemptions.’**  Previously, taxpayers would apply a reduction of taxable income of approximately $4000 each for themselves, their spouse, children as old as 24 and other specific individuals who qualified as dependents.  These exemptions have been eliminated.  In lieu of these reductions, an increase of almost double the **standard deduction** has been made.  For most taxpayer examples in this article, I use a married couple filing jointly (MFJ) situation, as being the most common filing method.  Where MFJ taxpayers in 2017 were eligible for a standard deduction from taxable income of $12,700, in 2018 that standard deduction is now $24,000.  Many people used to itemize deductions, however those who traditionally had itemized deductions which were more than the previously available deduction of $12,700 but less that the new deduction of $24,000, will likely no longer benefit from itemizing.  This means, State income and real estate taxes, mortgage interest, charitable contributions and employee-type expense deductions no longer matter.

For retirees now missing out on the deduction benefit of charitable contributions, you should remember the ability to make direct contributions from certain retirement plans.  (Google: “Qualified Charitable Distribution.”)

For those who still may have total itemized deductions more than the standard deduction of $24,000, **you can still itemize**, but other changes also apply.

- First, the Medical expense deduction still has a 'floor' or threshold which total expense needs to surpass before there is any deduction. This has been set back to 7.5% of Adjusted Gross Income (AGI) just for 2018. The threshold goes back to its previous 10% in 2019 and thereafter. And no longer do the 'over 65' crowd get a break in the floor.
- No longer are expenses, intended to encourage home-ownership as generous. The State and local tax (known as SALT) deductions, for state income tax, real estate taxes and personal property taxes are now maxed out at $10,000.
- Home mortgage interest is limited to a mortgage with an original principal less than $750,000, and interest on the Home Equity loan is no longer deductible.
- Charitable contributions deduction limit has been increased to 60% of AGI, but with elimination of the deduction for 'right to purchase tickets to athletic events.'
- Casualty losses are now restricted only to those covered by FEMA declaration
- Miscellaneous deductions are eliminated for tax years 2018 through 2025—these include Unreimbursed employee expense, including Home office; Union dues; Uniforms, tools and equipment; Investment Advisory, Tax Prep and Legal fees.
- Remaining substantially unchanged are Gambling losses (subject to changes in deducting expenses) and Impairment-related work expenses for disabled.

<u>Business owners</u>

For the broad category of ownership including proprietorship, partnership and shareholder in a Sub-chapter S Corporation, there is a new deduction against taxable income based on the "**flow through income**," or what is now referred to Qualified Business Income (QBI). QBI, defined under this new section 199A deduction, is used to determine a deduction of up to 20%, applied as another reduction from individual taxable income. (This does <u>not</u> reduce income subject to Self-employment taxes.)

Determination of this deduction is relatively straight-forward for MFJ returns with taxable income of less than $315,000 ($157,500 for single taxpayers). For returns over these thresholds, many more limitations are introduced, including the exclusion of this benefit for something call Specified Service Trade or Business (SSTB). The rules surrounding the definition of SSTB, and calculation of limitations become highly involved and fall in to the category of "do not try this at home!" But again, unless your total taxable income is over the thresholds, these additional limitations don't apply.

Other changes—

- Something called the **179 deduction**, which allows for the partial to full cost of newly acquired assets to be deducted in business returns, is now extended to **real estate rental enterprises**, and others filing Schedule E.
- Deduction of **entertainment expenses** is eliminated. **Meals**, must now include the business principal to take the usual 50% deduction

- Expenses of **in-office snacks and meals** now limited to 50% until 2025, at which time phase out to zero begins.

However, your business needs to be a legitimate trade or business (nothing new.) If the IRS finds you have been reporting business deductions for a period of time for what they deem to be a 'hobby,' you may get an unwanted tax bill.

<u>Other Business changes</u>
**Tax rates for corporations** (not Sub-chapter S) have been reduced to a flat 21%, from the previous bracketed rates of 15% to 35%. With the lower 15% bracket rate applicable up to $50,000 of taxable income, these corporations with this income and lower will now suffer an <u>increase</u> in tax rate, due to this change.

The benefit of corporate **exclusion of dividends** received from other corporations has generally been reduced, except for members of an affiliated group. The **corporate AMT** is eliminated. A new incentive benefit has been introduced for non –S corporations, of a credit of **12.5% of wages** paid to **employees on FML**A, where the amount being paid is at least 50% of normal compensation. This credit is increased to a maximum 25%, as the percentage of normal compensation increases above 50%.

For anyone involved with **non-profit organizations**, you may be interest to know that there a few subtle changes to these otherwise exempt entity tax laws.

- A new 21% excise tax is imposed on "excess" compensation of top executives paid more than one million dollars.
- A new 1.4% excise tax is imposed on the net investment income of certain private higher-ed schools.
- Income and losses from multiple **Unrelated Business** operations can no longer be offset
- And new excise taxes are imposed on certain **non-cash employee benefits** (e.g., parking lots and cafeterias).

<u>Implementation issues</u>
The significance of the changes and other considerations in the reformatting of IRS forms, has caused delays in publication of changes. In addition, the provisions of TCJA is having a secondary effect on State income tax rules, as many of them change to keep up. All of the changes to forms of IRS and States, once published, must be made to tax software programs used by individuals and professional tax preparers. Software companies believe these changes could be delayed until well into the tax filing season. Watch for what effect these delays might have on filing deadlines. And definitely, don't wait until the last minute to bring your papers to your trusty tax preparer.