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Open letter to all clients

On December 22, the President signed into law the Tax Cuts and Jobs Act of 2017 (TCJA). TCJA is the largest tax overhaul since the 1986 Tax Reform Act and it will affect almost every individual and business in the United States. Generally, the new law goes into effect in 2018, with many of the provisions relating to individuals expiring at the end of 2025.

I'm writing to give you a brief rundown of what's in the new law.

Overview of TCJA Changes Affecting Individuals

Tax Rates and Brackets. TCJA provides seven tax brackets, with most rates being two to three points lower than the ones under present law (the top rate goes from 39.6 percent to 37 percent). The top rate kicks in at $600,000 of taxable income for joint filers, $300,000 for married taxpayers filing separately, and $400,000 for all other individual taxpayers.While applicable rates at any given level of income generally go down by two to three points, some go up. For example, the rate for single individuals with taxable income between $200,000 and $400,000 goes from 33 percent to 35 percent.

Capital Gain Rates and Net Investment Income Tax. Tax rates on capital gains and the 3.8 percent net investment income tax (NIIT) are unchanged by TCJA.

Personal Exemptions and Standard Deduction. TCJA repeals the personal exemption deductions, but nearly doubles the standard deduction amounts to $24,000 for joint filers and surviving spouses, $18,000 for heads of household, and $12,000 for single individuals and married filing separately (additional amounts for the elderly and blind are retained).

Kiddie Tax Modified. The taxable income of a child attributable to earned income is taxed under the rates for single individuals, and taxable income of a child attributable to net unearned income is taxed according to the brackets applicable to trusts and estates. This rule applies to the child's ordinary income and his or her income taxed at preferential rates.

Exemption for Dependents and Child Tax Credit. Repeals the exemptions for dependents and increases the child tax credit to $2,000 maximum age for a child eligible for the credit remains 16 (at the end of the tax year).TCJA also provides a $500 nonrefundable tax credit for dependent children over age 16 and all other dependents.

Passthrough Tax Break. TCJA creates a new 20 percent deduction for qualified business income from sole proprietorships, S corporations, partnerships, and LLCs taxed as partnerships. The deduction is claimed by individuals on their personal tax returns as a reduction to taxable income. The new tax break is *subject to some complicated restrictions and limitations*, but the rules that apply to individuals with taxable income at or below $157,500 ($315,000 for joint filers) are simpler and more permissive than the ones that apply above those thresholds. (***Observation:*** The effective marginal tax rate on qualified business income for individuals in the top 37-percent tax bracket who are able to fully apply the new deduction will be 29.6 percent - fully 10 points lower than the top rate under current law.)

Deduction for State and Local Taxes. TCJA imposes a $10,000 limit on the deduction for state and local taxes, which can be used for both property taxes and income taxes (or sales taxes in lieu of income taxes

Mortgage Interest Deduction. TJCA reduces to $750,000 (from $1 million) the limit on the loan amount for which a mortgage interest deduction can be claimed by individuals, ***with existing loans grandfathered***. TCJA also repeals the deduction for interest on home equity loans. Generally, a future refinance will also be grandfathered if no addtional cash out occurs.

Deduction for Medical Expenses. TCJA lowers the adjusted gross income (AGI) floor for claiming the deduction from 10 percent to 7.5 percent for all taxpayers.

Deduction for Casualty and Theft Losses. TCJA repeals the deduction for casualty and theft losses, except for losses incurred in presidentially declared disaster areas.

Deduction for Charitable Contributions. Increases the maximum contribution percentage limit from 50 percent of a taxpayer's contribution base to 60 percent for cash contributions to public charities and certain private foundations.

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Overview of TCJA Changes Affecting Individuals (continued)

Deduction for Certain Miscellaneous Expenses. TCJA repeals the deduction for any miscellaneous itemized deductions subject to 2-percent of AGI floor.

Repeal of Alimony Deduction. TCJA repeals the deduction for alimony paid and also the corresponding inclusion in income by the recipient, effective for tax years beginning in 2019. Alimony paid under separation agreements entered into prior to 2019 will generally be grandfathered under the old rules.

Alternative Minimum Tax. TCJA increases alternative minimum tax (AMT) exemption amounts by 27 percent, and sharply increases the income level where the exemption is phased out.

Expanded Uses for 529 Plan Distributions. TCJA allows up to $10,000 in aggregate 529 distributions per year to be used for elementary and secondary school tuition. Under present law, 529 distributions can only be used for higher education expenses.

Repeal of Individual Healthcare Mandate. TCJA repeals the tax penalty on individuals who fail to carry health insurance enacted as part of the Affordable Care Act (ACA) effective ***after 2018***.

Estate and Gift Tax Exclusion. TCJA permanently doubles the basic exclusion amount for estate and gift tax purposes from $5.6 to $11.2 million.

Moving Expenses. For tax years beginning after Dec. 31, 2017 and before Jan. 1, 2026, the deduction for moving expenses is suspended, except for members of the Armed Forces on active duty who move pursuant to a military order and incident to a permanent change of station.