



January 3, 2018

Dear Client:

The tax reform legislation recently passed by Congress significantly changes the landscape for individuals beginning January 1, 2018, and continuing for many years to come. Due to the elimination or limitation on itemized deductions, and the elimination of personal exemptions, a key consideration in planning for 2018 is to first look at ways to lower your taxable income. (If applicable to you, see our separate letter addressing changes applicable to businesses.)

Also, despite the headlines, it will remain important for you to keep track of your medical expenses, mortgage interest, property and state income or sales tax payments and charitable contributions made during 2018, due to new restrictions on itemized deductions.

Highlighted below are some of the more significant changes made by the reform legislation and possible challenges and opportunities to lower your tax bill for 2018 and beyond.

Lower Individual Tax Rates — The legislation creates lower individual income tax brackets of 10%, 12%, 22%, 24%, 32%, 35%, and lowers the top rate from 39.6% to 37%, respectively. (The current rates would be restored in 2026, i.e., 10%, 15%, 25%, 28%, 33%, 35%, and 39.6%, respectively). The capital gain rates of 0%, 15% and 20% and the related income thresholds under prior law remain in effect.

Modification of the Alternative Minimum Tax (AMT) - The legislation retains the AMT for individuals but increases the exemption amount and phaseout thresholds so fewer people will pay it. From 2018 through 2025, a higher AMT exemption will apply to income, beginning with \$109,400 for joint filers and \$70,300 for other taxpayers in 2018. The exemption will phase out at \$1 million for joint filers and \$500,000 for other taxpayers. The thresholds will be adjusted for inflation.

Increase in the Standard Deduction — Beginning in 2018, the standard deduction increases significantly from \$12,700 to \$24,000 for joint filers, from \$9,350 to \$18,000 for heads of households, and from \$6,350 to \$12,000 for singles. Since you can claim the higher of the standard deduction or itemized deductions, you will want to closely compare the two methods as you may now benefit from a higher standard deduction given the many changes to itemized deductions.

Elimination of Personal Exemptions — In exchange for lower tax rates and increase in the standard deduction, personal exemptions no longer may be claimed beginning in 2018.

Child and Dependent Credits — From 2018 through 2025, the reform legislation increases the value of the child tax credit to \$2,000 per child under 17 from \$1,000. As much as \$1,400 of the credit will be refundable, thus allowing recipients to benefit even if they don't owe taxes. You will need to provide your child's Social Security number to claim the refundable portion through 2025. The refundable portion of the credit will be indexed for inflation. The legislation also expands eligibility for the credit by increasing the phaseout threshold to \$400,000 of adjusted gross income for joint filers (up from \$110,000 under current law), with a threshold for all other filers set at \$200,000. A \$500 nonrefundable credit for dependents other than children will be available through 2025.

\$10,000 Cap on State and Local Tax Deduction — In a significant departure from prior law, the legislation will allow individuals to deduct no more than \$10,000 of any combination of the following taxes - state and local income taxes, state and local property taxes, and sales taxes. This overall limitation



may result in the enhanced standard deduction yielding a larger deduction against your adjusted gross income and thus a lower tax bill.

Limits on Mortgage Interest Deduction — The tax reform act reduces the amount of mortgage indebtedness on which taxpayers may deduct interest to \$750,000 for mortgages incurred after December 15, 2017. (The \$1 million limitation remains for older debt). Interest on your principal residence and a second home are deductible. Importantly, however, beginning in 2018, interest on home equity indebtedness no longer is deductible, regardless of when it was incurred.

Medical Expense Deduction — Individuals may continue to deduct medical expenses in 2018 and 2019 if the expenses exceed 7.5% of adjusted gross income. The threshold returns to 10% of adjusted gross income in 2019. Again, you will need to review whether claiming such expenses, when combined with other allowable itemized deductions, yields a higher deduction than the standard deduction.

Charitable Contributions — The itemized deduction for charitable contributions remains in effect. However, the 50% of adjusted gross income limit is increased to 60%.

Elimination of Deduction for Unreimbursed Employee Business Expenses — The reform act eliminates the deduction for miscellaneous itemized deductions through 2025. Thus deductions (subject to the 2% of adjusted gross income floor) for costs related to the production or collection of income, such as appraisal fees, investment fees, and safety deposit box rent are now non-deductible, and, importantly, expenses related to employment, such as uniforms, professional society dues, computer used for work, and job-hunting expenses also are non-deductible. Employees who incur significant unreimbursed business expenses may want to ask their employer about adjusting their compensation or establish an accountable expense reimbursement plan that would allow the employer to reimburse the employee tax-free while also entitling them to a deduction against their business income.

Limitation on Itemized Deductions — The 3% reduction of itemized deductions for high income earners (the "Pease" limitation) is suspended under the 2017 Reform Act.

Affordable Care Act Individual Mandate — The "Obama Care penalty" for not having health care insurance is reduced to \$0 after 2018.

Tax Treatment of Pass-Through Entities and Sole Proprietorships — The 2017 Reform Act provides a 20% deduction for taxpayers that have "qualified business income" from partnerships, S-corporations and sole proprietorships.

Like-Kind Exchanges — Like-Kind exchange treatment is limited to exchanges of real estate. Previously this treatment was allowed for property held for productive use in a trade or business or property held for investment purposes.

If you have any questions or would like to discuss the new tax law, please contact us at your earliest convenience.

Sincerely,

Kruppa Nelson & Kovner, PLLC