PACIFIC WEALTH MANAGEMENT®

THE TAX CUT AND JOBS ACT OF 2017

Introduction

The *Tax Cut and Jobs Act of 2017* (2017)[1] is the most significant tax legislation since the *Tax Reform Act of 1986*. The law entails consequences for all taxpayers. Some of these consequences are beneficial, some are adverse. Below is a summary of the most significant changes organized by taxpayer category (individual, business, investor). These changes are further subdivided according to those who may be 'helped' and those who may be 'hurt' by the new law and what the net effect of this change is.

Individual Taxpayers

Individual taxpayers either take the standard deduction, which in 2018 is $24,000 for married filing jointly (MFJ) & $12,000 for filing single (S), or itemize their deductions. The IRS requires all taxpayers to utilize the greater of the two. In short, if your itemized deductions do not exceed the threshold of the standard deduction, you are required to use the standard deduction. The net effect of the TCJA is that only 12% of tax filers will now itemize their deductions, down from 31% prior to the change in law. Those who continue to itemize their deductions are likely to be impacted and those who itemize *and* live in states with high taxes are likely to be adversely affected by the new law.

Helped	Benefit
Itemizers who are residents of states with low taxes	Generally, wage earners from no-tax states could see tax savings.
Those with children age 16 and younger	Child Tax Credit increases from $1,000 to $2,000 per qualified child, with $1,400 being refundable. Phase out of credit begins at income of $200,000 (single) and $400,000 (married).
People with large estates	The applicable estate exclusion amount is doubled to $11,180,000 per person. As a result, far fewer individuals will be subject to estate tax.
High Earners	Top federal marginal tax rate reduced from 39.6% to 37%. In 2017 (old law), taxable income over $470,000 (MFJ) was taxed at 39.6%. In 2018 (new law), taxable income would need to be over $600,000 (MFJ) to be taxed at the highest federal marginal rate, now reduced to 37%.
Taxpayers who are subject to AMT	AMT exemption is increased allowing more taxpayers to avoid AMT.
Itemizers with high-income	Phase-out of itemized deductions is eliminated for high-income taxpayers. May allow higher income earners to continue itemizing and take full advantage of the deductions (i.e. higher dollar amount).
Itemizers who give large sums to charity	The charitable contribution ceiling is increased. A cash gift to public charities is now fully deductible up to 60% of a taxpayer's AGI.
Those who do not itemize their deductions	Standard Deduction increased to $24,000 (MFJ) / $12,000 (S).

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529 Education Savings account owners who pay for private K-12 school	The Act allows up to $10,000 per year from 529 accounts to be used for elementary and high school tuition and specifically allows funds to be used for private and religious schools.
People with disabilities	Rules related to ABLE contributions and rollover opportunities are enhanced. Contributions to ABLE accounts are eligible for the saver's credit. Contributions to ABLE accounts are increased to the amount of beneficiary's earned income (up to federal poverty line).
Those who desire tax filing simplification	The majority (88%) of Americans will now take the standard deduction, which reduces the burden of record keeping for the purposes of taking itemized deductions. The deduction item "personal exemptions" has been eliminated, replaced by an increased standard deduction and child tax credit.

Hurt	Loss
Itemizers who are residents of states with high taxes	Individual deduction for state and local (SALT) for income, sales, and property is limited in the aggregate to $10,000 (married, single, and head of household filers) resulting in potential tax increase.
Itemizers seeking to finance a home purchase in an expensive real estate market	Home buyers will no longer be able to deduct mortgage interest exceeding that attributable to a $750,000 mortgage. For example, if your mortgage is $1 million, only the interest attributable to $750,000 of that mortgage is deductible.
Itemizers seeking to use a HELOC for non-home-related expenses	Mortgage interest deduction is eliminated for interest paid on home equity debt, except for acquisition debt (buy, build, or improve your home) which is still deductible. Taxpayers can no longer use home equity loans to pay for personal expenses on a tax-advantaged basis.
Large Families	The deduction for personal and dependency exemptions have been repealed. Individuals with large families will see an increase in their taxable income. However, this may be mitigated or entirely offset by the increased standard deduction and/ or child credit.
Itemizers with large medical expenses	Starting in 2019, certain taxpayers may see reduced or eliminated deductions. Medical expenses were previously subject to a 7.5% AGI floor which will increase to $10,000 in 2019 meaning that only expenses exceeding 10% of AGI are deductible for itemizers.
Itemizers who sustain losses resulting from damage to personal property	Personal casualty losses are now limited to those losses incurred only on properties located within federally declared disaster areas. If the damage does not occur in a federally declared disaster area, it is no longer deductible.
Itemizers who sustain personal theft losses	Personal theft loss deduction is repealed.
Non-itemizers who tithe or are committed to charitable donations irrespective of tax benefit	If you are required to take the standard deduction, you cannot take an itemized deduction for charitable giving. Many of those who had previously benefited from the deductibility of charitable donations will lose the ability to do so under the standard deduction.

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Divorcing spouses	For payments required under divorce or separation instruments reached after December 31, 2018, the tax deduction for alimony payments is eliminated.
Those who wish to reverse a Roth IRA conversion	Under the new law, "re-characterizing" a Roth conversion that occurs in 2018 and beyond is no longer possible.
Those under 24 years of age with investment income	Unearned income of an individual either under age 19, or under age 24 and a full-time student, will be taxed at trust income tax rates. The result is a potential for increased tax for a given level of taxable income.

Businesses

Helped	Benefit
C Corporations	Tax rate reduced to flat rate of 21%
S Corporations, partnerships, and sole proprietorships	Taxpayers can deduct 20% of qualified business income received from flow-through entities (S corporations, partnerships, and sole proprietorships). *However*, if your business is a "specified service trade or business," (SSTB) and your taxable income is over a threshold amount, your pass-through deduction is gradually phased out.
Business owners who purchase, finance, or lease equipment	Taxpayers have an opportunity to take larger depreciation deductions on their business properties. Also, increased limits for expensing are allowed under Section 179 and certain real property improvements are added as qualifying property.
Hurt	**Loss**
Business owners who deduct meals and entertainment	Meal expenses are reduced up to 50%. ALL Business entertainment expenses eliminated.

Investors

Helped	Benefit
REIT investors	Reduced taxes on these income sources. Taxpayers can deduct 20% of income received from qualified REIT dividends, qualified cooperative dividends, and qualified publicly traded partnership income.
Hurt	**Loss**
Those utilizing like-kind exchanges for tax deferral	Limits applicability of like-kind exchanges to only real property that is not primarily held for sale. All other property previously eligible for 1031 like-kind exchange is no longer eligible (automobiles, equipment, and livestock).

[1] Tax Cut and Jobs Act of 2017, Pub. L. No. 115-97

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