What You Need to Know About the Incoming Tax Law

The tax reform legislation that Congress approved earlier this week was the largest change to the tax system in over 3 decades. The last time the U.S. tax code saw such a significant reform was under President Reagan in 1986. Those reforms sought to simplify income tax, broaden the tax base and eliminate many tax shelters.

Under this new legislation, substantial changes have been made to both individual and corporate tax rates. While most of the corporate provisions are permanent, the individual provisions technically expire by the end of 2025. There is speculation whether a future Congress will uphold the Individual provisions.

The new tax code contains many provisions that will affect individual, estate, and corporate taxpayers. To help you prepare, we have highlighted a few of the most pertinent details below. Please keep in mind, the purpose of this article is to summarize the key provisions.

What's Changing?

Tax Bracket Rates. While taxpayers will still fall into one of seven tax brackets based on their income, the rates have changed. Some of the brackets have been lowered. The new rates are: 10%, 12%, 22%, 24%, 32%, 35% and 37%.

Standard Deduction. The standard deduction has nearly doubled. For single filers it has increased from $6,350 to $12,000; for married couples filing jointly, it's increased from $12,700 to $24,000.

Personal Exemption. Under the prior tax code, a taxpayer could claim a $4,050 personal exemption for themselves, their spouse and each of their dependents, thus lowering their taxable income. Under the new tax code, the personal exemption has been eliminated. For some families, this will reduce or counter the tax relief they receive from other parts of the reform package.

State and Local Tax Deduction. The state and local tax deduction, or SALT, now has a cap. While it remains in place for those who itemize their taxes, it now has a $10,000 limit. This is a significant change as filers could previously deduct an unlimited amount for state and local property taxes, plus income or sales taxes.

The Child Tax Credit. The child tax credit has been expanded, doubling to $2,000 for children under 17. It's also available to more people. Single parents who make up to $200,000, and married couples who make up to $400,000 can claim the entire credit, in full.

Non-Child Dependents. A new tax credit is available for non-child dependents. Taxpayers, such as elderly parents, can claim a $500 temporary credit for non-child dependents. This can apply to a number of people adults support, such as children over age 17, elderly parents or adult children with a disability.

Alternative Minimum Tax. Fewer taxpayers will be affected by the alternative minimum tax. The purpose of the AMT is to ensure those who receive a lot of tax breaks are still paying some level of federal income taxes. The exemption will rise to $70,300 for singles, and to $109,400 for married couples.

Mortgage Interest Deduction. Going forward, anyone purchasing a home will only be able to deduct the first $750,000 of their mortgage debt. Down from $1 million, this will likely only affect people buying homes in more expensive regions. Current homeowners will likely be unaffected.

529 Savings Accounts. In the past, 529 savings accounts were untaxed and could only be applied towards college expenses. Under the new tax code, up to $10,000 can be distributed annually to cover the cost of sending a child to a public, private or religious elementary or secondary school.

Alimony Payment Tax Deduction. The tax deduction for alimony payments will be eliminated for couples who sign divorce or separation paperwork after December 31, 2018.

Moving Expenses Deduction. The tax deduction for moving expenses is also gone, but may be exceptions for members of the military.

Tax Preparation Deduction. Taxpayers can no longer deduct the cost of having their taxes prepared by a professional or the money they may have spent on tax preparation software.

Disaster Deduction. Under the prior tax code, losses sustained due to a fire, storm, shipwreck or theft that insurance did not cover and exceeded 10% of their adjusted gross income, were deductible. Effective under the new tax code, taxpayers can only claim the disaster deduction if they are affected by an official national disaster.

Estate Tax. Prior to the tax reform, a limited number of estates were subject to the estate tax, a tax which applies to the transfer of property after someone dies. Now, even fewer taxpayers will be affected. The amount of money exempt from the tax -- previously set at $5.49 million for individuals, and at $10.98 million for married couples -- has been doubled.

Health Insurance Mandate. The failure to repeal Obamacare earlier this year afforded the Republicans the opportunity to eliminate one of the health law’s key provisions with tax reform. Effective in 2019, the individual mandate, which penalized people who did not have health care coverage, was eliminated.

Corporate Tax Rate. Beginning in 2018, the corporate tax rate has been cut from 35% to 21%.

Pass-through Entities. The owners, partners and shareholders of S-corporations, LLCs and partnerships will receive a tax break. Those who pay their share of the business’ taxes through their individual tax returns will have a 20% deduction.
To ensure business owners do not abuse the provision, the legislation has included additional terms to this provision.

Multinational Corporations. The new tax bill is a shift towards globalization, changing the way multinational corporations are taxed. Companies will no longer pay federal taxes on income they make overseas. These companies will be required to pay a one-time, 15.5% on cash assets and 8% on noncash assets, on any existing offshore profits.

Nonprofit Organizations. There is a new 21% excise tax on nonprofit employers for salaries they pay out above $1 million.

Sexual Harassment Settlements. Companies can no longer deduct any settlements, payouts or attorney's fees related to sexual harassment if the payments are subject to non-disclosure agreements.

Bonus Depreciation. The Bonus depreciation will increase from 50% to 100% for property placed in service after September 27, 2017, and before January 1, 2023, when a 20% phase-down schedule will begin. The previous rule that made bonus depreciation available only for new properties was also removed.

Vehicle Depreciation. The new tax bill raises the cap placed on depreciation write-offs of business-use vehicles. $10,000 for the first year a vehicle is placed in service; $16,000 for the second year; $9,600 for the third year; and $5,760 for each subsequent year until costs are fully recovered. The new limits only apply to vehicles placed in service after December 31, 2017.

What's Staying the Same?

Student Loan Interest. You can still deduct Student Loan Interest – the deduction for this will remain max $2,500.

Medical Expenses. The deduction for medical expense was untouched. Rather, it was expanded by two years. Filers can deduct medical expenses that exceed 7.5% of their adjusted gross income.

Teachers. Teachers will continue to deduct up to $250 to offset what they spend on resources for the classroom.

Electric Car Credit. If you drive a plug-in electric vehicle, you can still claim a credit of up to $7,500.

Home Sellers. Homeowners that sell their house and make a profit can exclude up to $500,000 (or $250,000 for single filers) from capital gains. This is still requires that it is their primary home and they have lived there for at least two of the past five years.

Tuition Waivers. Tuition Waivers, typically awarded to teaching and research assistants, will remain tax free.

What Does This All Mean?

Although doubling the standard deduction will arguably simplify the process of filing taxes for individuals, there are still deductions and credits to consider. More so, the filing for small businesses, can potentially become more complicated. Depending on your situation, it may be beneficial to review your filing status as part of an overall tax planning strategy.

Again, please keep in mind that the purpose of this article is to summarize the key provisions. Each client scenario will be different and this has to be taken into account. The professionals in our office can answer the questions you may have regarding the individual, estate and corporate tax provisions outlined in the Republican's tax reform bill, call us today.