A Summary Of Tax Law Changes

Summary

- The Tax Cuts and Jobs Act has substantially changed tax law.
- The Bipartisan Budget Act has also provided change to the tax code.
- This article summarizes all tax law change that will affect households.

On December 22, 2017, President Trump signed into law the Tax Cuts and Jobs Act (TCJA) of 2017, most of which will affect our taxes and those of U.S. business beginning 2018. This tax law change will affect all taxpayers. Most will experience a tax reduction, although some will see an increase.

To better explain the TCJA in plain English, I break the tax return down into 4 sections:

1. Income
2. Deductions
3. Tax computation
4. Credits

The following are the changes the TCJA brings to these sections for households filing tax returns:

Income: No change. What was income before is income under the TCJA.

Deductions: Significant changes. Deductions can be broken down into 3 categories: Above the Line (ATL), Itemized or Standard and the Personal Exemption. Let's look at each separately.

- ATL deductions are taken on the front of the 1040 tax form such that the taxpayer does not have to itemize them (on schedule A) to be able to take them. ATL deductions will not change for 99% of taxpayers. The two changes are the elimination of the moving expense (except for military) and the elimination of alimony both as a deduction and income beginning 2019. The Tuition & Fees deduction has been reinstated under a separate legislative act but only for 2017. All other ATL deductions remain unchanged.

- The Greater of the Itemized or Standard Deduction: Here change to the household's tax return is certain. Some will see a modest change while for many households, the change will be substantial:
    - Standard deduction doubles from $6,350/$12,700 in 2017 for Single (NYSE:S)/Married Filing Jointly (MFJ) to $12,000/$24,000. The added $1,600/$1,300 for S/MFJ who are 65 and older or anyone who is blind, remains. So under the TCJA, the Standard Deduction for a couple age 65 and older increases from $15,200 in 2017 to $26,600 in 2018.
    - Itemized Deduction: These are deductions taken on Schedule A and when totaled, are used only if this total exceeds the household’s standard deduction. There are 7 Itemized Deductions that are affected under the TCJA
        1. Combined State Tax (or sales tax for those states without a state tax) and property tax are limited to $10,000 for both S and MFJ. This may have a profound reduction in itemized deductions in high income tax states, such as CA, NY or OR. For example, in OR, a couple MFJ with an Adjusted Gross Income (NYSE:AGI) of $150,000 and two children will have a state tax in the $11,000 to $13,000 range. Add this to their property tax of, say, $4,000, means in 2017 this provided a deduction of $15,000 to $17,000....but this will be reduced to a maximum deduction of $10,000 under the TCJA beginning in 2018.
        2. Loss of casualty/theft loss deduction except for Presidential declared disasters.
        3. Loss of Miscellaneous Itemized Deductions in excess of 2% of AGI. This may be significant to those households who pay an investment advisor and a tax preparer. For example, a retired household with $100,000 AGI and $1MM in IRAs with an investment advisory fee of 1% per year, and a $500 charge for tax preparation each year, will have an itemized gross expense of $10,000 + $500 = $10,500. The 2% of AGI threshold = $2,000, so the deductible amount would be $8,500, which will be lost beginning 2018. Another group affected will be employees who pay much of their own professional costs, such as professional memberships/certifications, employment related education, union dues or other non-reimbursed employment-related expenses.
        4. Medical expenses deduction is only one of two deduction that will increase for 2017 and 2018. The medical deduction resets the threshold to 7.5% instead of 10% of AGI. This will be beneficial to households with moderate incomes but with large medical/drug costs AND high insurance premiums.

5. Home Equity Loan interest (for loans up to $100,000 that are not used to substantially improve the residence) are repealed
6. Homes purchased after December 15, 2017, principal residence and a second home, combined, deductible mortgage interest is limited to a mortgage(s) maximum of $750,000.
7. The maximum cash charitable contribution that is deductible will increase from 50% of AGI to 60% of AGI. Annual cash donations this large are unusual and will most likely occur with contributions of highly appreciated securities to a Donor Advised Fund.

- Personal Exemptions: This deduction is repealed. The loss of this deduction can be profound at $4,150 per individual (This is what the personal exemption would have been in 2018 had the TCJA not passed). All households will experience the loss of this deduction. For a household of 5, this is a loss of $20,750 in deductions.
- Phase out of itemized deductions and personal exemptions. Called the Pease Reduction, has been repealed. The Pease Reduction phased out itemized deductions and personal exemptions at an AGI of $266,700/$320,000 for S/MFJ.