

The Kiplinger Tax Letter

SPECIAL
NEW TAX RULES
FOR 2018

CIRCULATED BIWEEKLY TO BUSINESS CLIENTS SINCE 1925

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Dear Client:

Washington, Dec. 29, 2017

Big changes are going into effect in 2018...
Thanks to the massive new tax legislation
that Republican lawmakers enacted at warp speed.
Most changes won't affect 2017 returns filed next year.
This Letter is devoted to the new law.

Most individual tax provisions are temporary.
They expire after 2025. Unless extended
by another Congress, the provisions will revert
automatically to the rules now in effect for 2017.
Corporate tax changes are made permanent.

HIGHLIGHTS

Tax Brackets	New brackets
Investments	Capital gains rates
Minimum Tax	Higher exemptions
Health Care	Individual mandate
Business Taxes	21% corporate rate
Exempt Groups	Excise tax

PERSONAL TAXES

Let's start with individual taxes. Standard deductions nearly double
to \$24,000 for couples, \$12,000 for singles and \$18,000 for household heads.
Folks age 65 or up and blind people get \$1,250 more per person (\$1,550 if unmarried).
Given these much higher amounts, it's a sure bet that far fewer people will itemize.

The new law pares back or axes many deductions claimed by individuals.
Personal exemptions for individual filers and their dependents are repealed.
Home mortgages are nicked. Interest can be deducted on up to \$750,000
of new acquisition debt on a primary and second residence...down from \$1 million.
The new limit generally applies to mortgage debt incurred after Dec. 14, 2017.
Older loans...and refinancings up to the old loan amount...get the \$1-million cap.
No write-off is allowed after 2017 for interest on existing or new home equity loans.

The popular deduction for state and local taxes is being squeezed.
You can deduct any combination of residential property taxes and income or sales taxes
up to a \$10,000 cap. Property taxes remain fully deductible for taxpayers in a business
or for-profit activity, so taxes paid on rental realty can be taken in full on Schedule E.

Several other write-offs are eliminated: Deductions for job-related moves,
except for the military. All miscellaneous write-offs subject to the 2%-of-AGI threshold,
including employee business expenses, brokerage and IRA fees, hobby expenses
and tax return preparation costs. Theft losses. Alimony for post-2018 divorce decrees,
although it's good news to recipients, who will not be taxed on alimony they receive.
Plus personal casualty losses, excluding those in presidentially declared disaster areas.

The charitable contribution write-off is preserved, with some changes.
The AGI limitation on cash donations to qualified charities is hiked from 50% to 60%.
But gifts to colleges in exchange for choice seating rights at athletic events are targeted.

The medical expense deduction is enhanced. Not only have lawmakers opted
to keep this popular write-off, but they've also temporarily lowered the AGI threshold
for deducting 2017 and 2018 medical expenses on Schedule A from 10% to 7.5%.

The write-off for personal gambling losses to the extent of winnings survives.

Upper-income individuals can finally say good-bye to a sneaky tax hike:
The phaseout of itemized deductions is scrapped under the new law.

TAX BRACKETS

The law keeps seven tax brackets, but with different rates and break points. For example, not only is the top individual rate lowered from 39.6% to 37%, but that rate kicks in at a higher income level. And, note that whatever new bracket you fall into, more of your taxable income will be hit with lower rates than before.

Marrieds: If taxable income is	The tax is
Not more than \$19,050	10% of taxable income
Over \$19,050 but not more than \$77,400	\$1,905.00 + 12% of excess over \$19,050
Over \$77,400 but not more than \$165,000	\$8,907.00 + 22% of excess over \$77,400
Over \$165,000 but not more than \$315,000	\$28,179.00 + 24% of excess over \$165,000
Over \$315,000 but not more than \$400,000	\$64,179.00 + 32% of excess over \$315,000
Over \$400,000 but not more than \$600,000	\$91,379.00 + 35% of excess over \$400,000
Over \$600,000	\$161,379.00 + 37% of excess over \$600,000

Singles: If taxable income is	The tax is
Not more than \$9,525	10% of taxable income
Over \$9,525 but not more than \$38,700	\$952.50 + 12% of excess over \$9,525
Over \$38,700 but not more than \$82,500	\$4,453.50 + 22% of excess over \$38,700
Over \$82,500 but not more than \$157,500	\$14,089.50 + 24% of excess over \$82,500
Over \$157,500 but not more than \$200,000	\$32,089.50 + 32% of excess over \$157,500
Over \$200,000 but not more than \$500,000	\$45,689.50 + 35% of excess over \$200,000
Over \$500,000	\$150,689.50 + 37% of excess over \$500,000

Household Heads: If taxable income is	The tax is
Not more than \$13,600	10% of taxable income
Over \$13,600 but not more than \$51,800	\$1,360.00 + 12% of excess over \$13,600
Over \$51,800 but not more than \$82,500	\$5,944.00 + 22% of excess over \$51,800
Over \$82,500 but not more than \$157,500	\$12,698.00 + 24% of excess over \$82,500
Over \$157,500 but not more than \$200,000	\$30,698.00 + 32% of excess over \$157,500
Over \$200,000 but not more than \$500,000	\$44,298.00 + 35% of excess over \$200,000
Over \$500,000	\$149,298.00 + 37% of excess over \$500,000

Inflation indexing of income tax brackets and various tax breaks is altered.

Tax brackets, standard deductions and many other items will be adjusted annually using a chained consumer price index, resulting in lower inflation adjustments and thus smaller annual increases than with the current index. According to critics, this is a hidden tax hike that over time will nail nearly all individual filers.

INVEST-MENTS

Tax rates on long-term capital gains and qualified dividends do not change.

Currently, your capital gains and dividends rate depends on your tax bracket. But with the bracket changes, Congress decided to set income thresholds instead. The 0% rate will continue to apply for taxpayers with taxable income under \$38,600 on single-filed returns and \$77,200 on joint returns. The 20% rate starts at \$425,800 for singles and \$479,000 for joint filers. The 15% rate applies for filers with incomes between those break points. The 3.8% surtax on net investment income remains, kicking in for single people with modified AGI over \$200,000...\$250,000 for marrieds.

MINIMUM TAX

The law keeps the individual alternative minimum tax with higher exemptions:

\$109,400 for joint return filers and \$70,300 for singles and household heads. Additionally, the exemption phaseout zones start at much higher income levels... above \$1 million for couples and \$500,000 for single people and heads of household.

HEALTH CARE

Obamacare's individual mandate is on the way out. The requirement

that folks have health insurance, qualify for an exemption, or pay a fine is repealed for post-2018 years. Keep in mind the mandate continues to apply for 2018.



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TAX CREDITS

The child tax credit is doubled to \$2,000 for each dependent under age 17, with up to \$1,400 of the credit refundable to lower-income taxpayers.

The income phaseout thresholds are much higher...AGIs over \$400,000 for couples and \$200,000 for all other filers. A Social Security number is needed for each child.

There's a new \$500 credit for each dependent who is not a qualifying child, including, for example, an elderly parent you take care of or a disabled adult child. It's nonrefundable and phases out under the same thresholds as the child credit.

ESTATES & TRUSTS

Far fewer estates will be subject to the estate tax, now that Congress has doubled the lifetime estate and gift tax exemption to about \$11 million.

The rate remains 40%. The annual gift tax exclusion for 2018 is \$15,000 per donee.

There's no change in the asset basis step-up for heirs of estates of any size.

The income tax rates and brackets for trusts and estates have been revised.

If income of an estate or trust is

Not over \$2,550

Over \$2,550 but not more than \$9,150

Over \$9,150 but not more than \$12,500

Over \$12,500

The income tax is

10% of taxable income

\$255 plus 24% of excess over \$2,550

\$1,839 plus 35% of excess over \$9,150

\$3,012 plus 37% of excess over \$12,500

KIDDIE TAX

The kiddie tax is significantly revamped, so that unearned income

of children will be taxed at the ordinary income and capital gains rates

applicable to trusts and estates, and not at their parents' marginal tax rate, as before.

SAVINGS PLANS

Generally, tax benefits for retirement savings haven't been curtailed.

There is an important change involving Roth IRA conversions, however.

The new law bars IRA owners who convert their traditional IRAs to Roth IRAs from later undoing the conversion and recovering the income tax paid on the switch.

529 college savings plans are enhanced to allow annual distributions of up to \$10,000 per student to pay tuition for elementary and secondary education.

There are favorable changes to ABLE savings programs for the disabled.

The new law allows limited tax-free rollovers from 529 plans to ABLE accounts.

It also lets ABLE account beneficiaries make contributions to their accounts over the \$15,000 annual payin limit. These payins are eligible for the saver's credit.

BUSINESS TAXES

The new tax law dramatically reforms the taxation of businesses of all sizes.

Regular corporations ("C corporations") will pay tax at a flat 21% rate,

down from the 35% top rate now. This lower rate begins in 2018 and is permanent.

Unlike the individual AMT, lawmakers killed the corporate AMT altogether.

Many individual owners of pass-throughs will get a new 20% deduction.

The rules cover sole proprietors and owners of S corporations, partnerships and LLCs. REIT shareholders and partners in publicly traded partnerships also get the break.

They can generally deduct 20% of so-called qualified business income.

These provisions are, however, some of the most complex in the new law.

There are lots of limits and restrictions to help deter gaming of the tax system.

The break phases out for high earners in professional service fields,

such as law, consulting, accounting, health or financial services, with taxable incomes in excess of \$315,000 for joint returns and \$157,500 for all other taxpayers.

The deduction for business losses on individual returns is capped.

The amount of trade or business losses that exceed a \$500,000 threshold for couples and \$250,000 for other filers is nondeductible, but any excess can be carried forward.

Note this limitation applies after application of the current passive-activity loss rules.



**MORE
BUSINESS**

There are enhanced write-offs for business asset purchases in the law.
100% bonus depreciation for many assets put into use during the year.
The break applies to assets put in service after Sept. 27, 2017, and is temporary...
generally lasting until 2022 and then phasing out 20% each year thereafter.
A higher cap on expensing business assets. It doubles to \$1 million.
More property is eligible for first-year bonus depreciation or expensing.
Depreciation limitations on passenger automobiles are increased.

The deduction that firms claim for interest on business debt is limited.
Their net interest write-offs will be capped at 30% of adjusted taxable income,
with disallowed interest carried forward. Firms with \$25 million or less of gross receipts,
real estate companies and certain regulated public utilities will be exempt.

Among the many other business breaks that are eliminated or pared back:
Business entertainment. Country club dues. The 9% domestic production deduction.
Net operating losses can offset only 80% of taxable income, and NOL carrybacks
are generally prohibited. Tax-deferred like-kind exchanges are limited to real property
not held primarily for sale. Sexual harassment settlement payments aren't deductible
if subject to a nondisclosure agreement. Plus the write-off for local lobbying expenses.

Some popular deductions for fringes are also scrapped or limited.
The write-off that employers take for the cost of transportation-related fringe benefits,
such as parking, mass transit passes and even bicycle commuting, is disallowed.
Employees can still use pretax money for parking and transit passes, but not biking.
Meals in on-premises dining facilities such as cafeterias are subject to a 50% bite
through 2025...the deduction is fully axed in later years. The rehab credit is revised.

Firms that provide paid family or medical leave to workers get a new credit
generally equal to 12.5% of the amount of wages paid during the period of leave.
The credit is increased for employers that pay workers over half their normal wages
while on leave. Note that there are lots of other rules and limitations to comply with.
There's a catch. The credit is temporary...applying only for 2018 and 2019.

The law includes a revenue-raising provision on U.S. multinationals:
A one-time low tax on previously untaxed accumulated overseas earnings.
The rate is 15.5% on foreign cash and liquid assets and 8% on other reinvested profits.

There are many more tightenings for certain businesses...insurers, banks, etc.
And easings for others...S corporations, farmers, craft brewers and more.

**EXEMPT
GROUPS**

Exempt organizations aren't left untouched. Among the changes:
Private colleges with very large endowments would pay a 1.4% excise tax
on net investment income. The tax applies to schools with at least 500 students
and non-education-related assets valued at \$500,000 or more per full-time student.

**HERE
TO HELP**

We trust you will find our broad-brush summary of the new law helpful.
The bill is hundreds of pages, and we only just touched the surface here.
You can bet that we'll cover various aspects of the law in more detail in future Letters.
We work entirely for you, the reader. So call or send an e-mail if you have questions.

Yours very truly,

The Kiplinger Editors
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