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The Tax Cuts and Jobs Act
How will it affect your tax bill?

At the end of 2017, the most sweeping tax reform legislation in decades was signed into law. Let's take a look at the highlights of the Tax Cuts and Jobs Act (TCJA) that affect individuals and businesses. Most of the changes go into effect this year.

Individual taxes

As under previous law, there are seven individual tax brackets, but the tax rates have been adjusted to 10%, 12%, 22%, 24%, 32%, 35% and 37%. The previous rates were 10%, 15%, 25%, 28%, 33%, 35% and 39.6%. (Long-term capital gains rates haven't changed and remain at 0%, 15% and 20%.)

The TCJA also adjusts the income thresholds for each bracket. For example, the top rate of 37% applies to 2018 taxable income over $500,000 for single filers and $600,000 for married couples filing jointly. For 2017, the 39.6% rate kicked in at income levels of $418,400 and $470,700, respectively.

Most taxpayers will enjoy a tax cut under the new law, but not everyone. For example, a married couple filing jointly with $500,000 in taxable income will see their marginal rate drop from 39.6% to 35%. On the other hand, the marginal rate for a single filer with $180,000 in taxable income will increase from 28% to 32%.

The TCJA also makes many changes that affect taxable income, including:

- Nearly doubling the standard deduction to $12,000 for single filers and $24,000 for joint filers,
- Eliminating personal exemptions,
- Boosting the child tax credit, and
- Generally reducing itemized deductions by:
    - Capping the deduction for state and local taxes (on a combined basis for property tax and either income or sales tax) at $10,000,
    - Limiting the deduction for home mortgage interest to indebtedness up to $750,000 for new mortgages,
    - Generally eliminating the deduction for interest on home equity debt,
    - Eliminating the deduction for casualty and theft losses except for losses due to an event officially declared a disaster by the President, and
    - Eliminating the miscellaneous itemized deduction for expenses such as investment expenses, certain professional fees and unreimbursed employee business expenses.

The TCJA does enhance a couple of deductions. It increases the adjusted gross income (AGI) limit on the deduction for cash charitable contributions from 50% to 60%. And it reduces the AGI threshold for medical expense deductions to 7.5% for 2017 and 2018, reverting to 10% in 2019.

A key consideration for 2018 tax planning is whether to itemize or take the standard deduction. Many taxpayers who've typically itemized in the past will find they're better off taking the standard deduction because their itemized deductions will be lower than that amount.

One potential strategy is to "bunch" your charitable contributions. Say you file a joint return and your itemized deductions consist of $10,000 in state and local taxes and $10,000 in charitable contributions. Because your itemized deductions are less than $24,000, it makes sense to take the standard deduction. You can increase your deductions, however, by contributing $20,000 to charity every other year, allowing you to deduct $30,000 in those years and $24,000 in the off years.

Keep in mind that most of the TCJA's individual tax changes are temporary — they're scheduled to expire at the end of 2025.

Business taxes

The TCJA *permanently* reduces the corporate income tax to a flat 21% rate. Previously, C corporations were subject to graduated tax rates ranging from 15% to 39%, with a 35% marginal rate for the highest income tax bracket. In addition, the new law eliminates the corporate alternative minimum tax (AMT).

The TCJA also provides relief to pass-through entities — S corporations, partnerships, limited liability companies and sole proprietorships — by allowing them to deduct 20% of their qualified business income (for an effective top marginal rate of 29.6%). Note, however, that the deduction may be reduced or eliminated for pass-through owners whose taxable income exceeds $157,500 for single filers or $315,000 for joint filers. Above those thresholds, the deduction becomes unavailable to certain service businesses and is subject to limits based on a business's W-2 wages and depreciable assets.

Depending on their circumstances, some businesses may benefit by converting from pass-through to C corporation status, or vice versa. However, be aware that the pass-through entity deduction is scheduled to expire after 2025.

Review your plan

The TCJA will have an impact on nearly every individual and business, and we've just scratched the surface of the wide-ranging changes the act makes. For example, the new law also increases the AMT exemption for individuals and makes significant changes to various business tax breaks, enhancing some and reducing or eliminating others. Contact your tax advisor to discuss what the TCJA will mean for your tax bill and how you can take advantage of planning opportunities.

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Sidebar: TCJA provisions that affect estate planning

The Tax Cuts and Jobs Act doubles the combined gift and estate tax exemption and the generation-skipping transfer (GST) tax exemption from $5 million to $10 million (adjusted for inflation) for deaths and gifts after 2017 and before 2026. The inflation-adjusted exemption amounts for 2018 are expected to be $11.2 million ($22.4 million for married couples if they plan properly).

This creates an excellent opportunity to “lock in” the higher exemption amounts by accelerating lifetime gifts and creating dynasty trusts.

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